

REPORT BY THE STATE AUDITOR OF CALIFORNIA

**CONTINUED IMPROVEMENT NEEDED IN THE
STATE'S CONTROLS OVER ITS OPERATIONS**

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**Continued Improvement Needed In the
State's Controls Over Its Operations**

93002, June 1994

**California State Auditor
Bureau of State Audits**



CALIFORNIA STATE AUDITOR

BUREAU OF STATE AUDITS

KURT R. SJOBERG
State Auditor

June 30, 1994

MARIANNE P. EVASHENK
Chief Deputy State Auditor

93002

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Governor and Legislative Leaders:

The Bureau of State Audits presents the results of our review of the State's control of its financial activities and its compliance with federal grant requirements and state regulations. This review was made as part of our examination of the State's general purpose financial statements. This report fully meets the requirements of the 1984 Single Audit Act set forth by the United States Government as a condition of receiving more than \$19 billion in federal funds annually. The Bureau of State Audits, which was created in May 1993, pursuant to California Government Code, Section 8543, is responsible for performing the annual financial and compliance audit previously conducted by the Office of the Auditor General.

The State continues to need improvement in its accounting, auditing, and administrative control structure. For example, we found numerous inadequacies in the State's monitoring of recipients of state and federal moneys. As a result, the State cannot ensure that the recipients are complying with regulations or laws governing the receipt or use of these moneys. In addition, we noted instances in which the State failed to promptly bill for costs incurred, resulting in lost interest earnings or an impairment in the State's ability to collect amounts owed to the State.

In responding to weaknesses we have reported in an earlier audit, the State has made some improvements in its internal control structure. For example, the Office of Local Assistance now has a system in place to ensure that local educational agencies report interest earned on advances from the State for construction projects. In August 1993, \$25 million of this earned interest was transferred to the State's General Fund.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Kurt Sjoberg".

KURT R. SJOBERG
State Auditor

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Summary

The State continues to have many weaknesses in its accounting, auditing, and administrative control structure. The weaknesses, which we found in numerous departments, result in inaccurate financial statements, noncompliance with state and federal regulations, and waste, loss, and misuse of state resources. Most of these weaknesses individually have a minor effect on the State's operations, but their cumulative effect can be significant. Following are some of the more significant weaknesses we found.

- The Department of Transportation lost approximately \$972,000 in interest earnings because of \$6 million in late billings we reviewed. The billings were to the federal government for costs the State incurred. We did not calculate interest lost on an additional \$5 million in late billings at the Department of Transportation, but we estimate lost interest would not exceed \$808,000.
- As of October 26, 1993, the Office of Emergency Services had not appealed the Federal Emergency Management Agency's denial of approximately \$7.7 million of claimed expenses related to the Loma Prieta earthquake even though the office indicated that it intended to make its appeal by May 29, 1992.
- The Department of Health Services did not have adequate procedures for monitoring and collecting almost \$240 million in accounts receivable. In addition, the department did not adequately distribute responsibilities among its staff for activities related to accounts receivable.
- The Department of General Services has not audited within the required three years 80 of the 151 departments to which it delegated purchase authority totaling more than \$214 million as of August 1993.
- The Department of Finance allowed certain departments to use funds that would have been available for future General Fund expenditures. As a result, the State has approximately \$16.5 million less for future General Fund expenditures than originally anticipated. In addition, because not all General Fund departments were treated in a uniform manner, these departments were afforded a benefit not provided to other General Fund departments.

- During fiscal year 1992-93, the Office of Emergency Services did not promptly collect \$183,350 in overpayments made to five recipients of disaster assistance funds. Office records indicate that other applicants owe an additional \$900,000. Some of these debts date back to 1987.
- The State did not fully comply with federal regulations in 28 of the 46 major grants we reviewed.
- The Stephen P. Teale Data Center has not attempted to collect approximately \$14 million in undercharges to the Department of Motor Vehicles from prior years and approximately \$94,000 in undercharges to the Governor's Office from prior years.
- The State does not recognize the liability for earned vacation credit in its budgetary basis financial statements. As of June 30, 1994, the liability was \$1 billion.
- The Student Aid Commission did not ensure that credit bureaus accurately recorded information about defaulted student loans. For 10 of the 12 loans we reviewed, either one or two of the three credit bureaus to which the commission reports had no record of the defaulted loans.
- The California Museum of Science and Industry in Los Angeles has inadequate controls over cash receipts for parking for special events. The cash receipts amounted to more than \$48,000 during fiscal year 1992-93. The same person controls and accounts for sequentially numbered parking tickets and collects and accounts for the cash, leaving the receipts vulnerable to errors, irregularities, or illegal acts that may go undetected for extended periods.
- The State has numerous deficiencies in its monitoring of recipients of state or federal moneys. We found 19 federal programs in eight departments deficient in required monitoring practices. Without adequate monitoring of recipients of state and federal moneys, the State cannot ensure that the recipients are complying with regulations or laws governing the receipt or use of these moneys.
- The Department of Housing and Community Development did not follow state regulations for the purchase of electronic data processing equipment exceeding \$100,000. The department used

nine separate purchase invoices so that no one order exceeded the 100,000 threshold for review by the Department of General Services.

- The Stephen P. Teale Data Center could not provide records, including those identifying amounts owed by individual clients, to support \$18.6 million in amounts due from other funds. In addition, the data center could provide no supporting documentation for \$2.4 million in contracts payable.
- The Office of Criminal Justice Planning purchased more than \$840,000 of computer equipment with federal grant moneys when the purchase was not authorized in the grant agreement. In addition, the department could not provide evidence of other authorization for the purchase. As a result, the office may be liable to the federal government for the unauthorized expenditures.

We noted these deficiencies during our annual financial and compliance audit of the State. Procedures we perform during this audit include evaluating internal controls over activities that can directly affect the financial statements or controls that are required for the receipt of federal funds. The audit does not directly deal with the economy, efficiency, or effectiveness of the State's administration although such issues may arise during our audit.

Although these weaknesses exist in the State's control structure, the State has made significant improvements in certain areas as a result of its response to weaknesses the Bureau of State Audits and the Office of the Auditor General have reported.¹ Following are examples of some of these improvements.

- For fiscal year 1990-91, the Office of the Auditor General reported that the Office of Local Assistance (office) did not have an adequate system in place to ensure that local educational agencies reported interest earned on advances from the State for construction projects. By fiscal year 1992-93, the office had corrected this deficiency. As a result, during fiscal year 1992-93, the office identified a total of \$58.4 million in interest earnings for fiscal years 1984-85 through 1991-92, \$39.6 million of which represented previously

¹ The Office of the Auditor General was closed in December 1992. The California Government Code, Section 8543, creates the Bureau of State Audits. The Bureau of State Audits is responsible for performing the annual financial and compliance audit of the State and other audits formerly conducted by the Office of the Auditor General.

unidentified interest through June 30, 1991. In August 1993, the office transferred \$25 million of these interest earnings to the State's General Fund.

- From fiscal year 1988-89 through fiscal year 1991-92, the Office of the Auditor General or the Bureau of State Audits reported that the Stephen P. Teale Data Center did not charge all state agencies based on its published rate schedule. For example, the data center undercharged the Department of Motor Vehicles approximately \$14 million over four years, resulting in a disproportionate share of the data center's costs being passed on to other funds, including the State's General Fund. For fiscal year 1992-93, we found no further instances where this occurred.

Introduction

As part of our examination of the general purpose financial statements of the State of California for fiscal year ended June 30, 1993, we studied and evaluated the State's internal control structure. The purpose of our study of this structure was to determine the audit procedures and the extent of testing necessary for the following three reasons:

- Expressing an opinion on the State's general purpose financial statements;
- Determining compliance with federal grant requirements, laws, and regulations; and
- Determining compliance with state laws and regulations that could materially affect the general purpose financial statements.

In conducting our audit, we reviewed and evaluated fiscal controls at 20 of the 196 state agencies included in the general purpose financial statements.

Amounts that we audited at these agencies represented approximately 73 percent of the State's additions to funds and approximately 67 percent of the State's deductions from funds. Further, other independent auditors audited an additional 19 percent of the State's additions and an additional 13 percent of the State's deductions. We increased our coverage with centralized testing, which we performed by selecting for review a cross section of items from the State as a whole. For example, we selected a sample of payroll warrants the State processed through its payroll system, and we selected a sample of warrants other than payroll warrants that the State processed through its claims payments system. We also reviewed electronic data processing activities at selected state agencies that have significant data processing operations.

We performed a limited review of the internal audit units at four state agencies. We noted no significant variances from the Standards for the Professional Practices of Internal Auditing. Based on the results of our review, we concluded that the internal audit activities were reliable.

We reviewed 14 agencies' compliance with state laws and regulations that materially affect the State's financial statements. Compliance with these laws and regulations helps to ensure that the State maintains sufficient control over the budgeting, investing, collecting, and disbursing of state money and that it maintains sufficient control over reporting the results of state financial activities.

Finally, except for the financial aid programs administered by the California State University and federal grants administered by the University of California, which are reviewed by other independent auditors, we reviewed the State's compliance with federal regulations for all federal grants exceeding \$20 million. In all, we reviewed 46 of the 323 federal grants the State administers. These 46 grants represent approximately 97 percent of the federal funds the State received in fiscal year 1992-93, excluding most financial aid funds the California State University received and those funds the University of California received. In addition, as part of our examination of the State's financial statements, we selected transactions related to other federal programs and reviewed these transactions for compliance with applicable federal regulations.

The specific scope of our audit is stated in the following reports that the federal Office of Management and Budget, Circular A-128, requires the State to issue each year:

- The report on the internal control structure used in preparing the general purpose financial statements and in administering federal assistance programs (begins on page 33);
- The report on weaknesses and instances of noncompliance at state agencies (begins on page 39);
- The report on federal assistance programs, including required reports on (1) compliance with laws and regulations related to major and nonmajor federal programs (begins on page 165) and (2) the resolution of prior year findings related to federal programs (begins on page 165);
- The report on the accuracy of the supplementary schedule of federal assistance (begins on page 171); and
- The report on compliance with state laws and regulations (begins on page 213).

Between July 1, 1992, and December 31, 1993, the Bureau of State Audits and the Office of the Auditor General issued 15 audit reports, many of which discussed improvements needed in the State's operations. These reports, listed in the Appendix, are available to the public through the Bureau of State Audits.

Statewide Concerns

Summary The State has numerous weaknesses in its control system that warrant statewide concern. Such weaknesses have one or more of the following characteristics.

- They exist at numerous departments throughout the State.
- They arise from current statewide policies that do not satisfactorily address the State's needs.
- They have a potentially significant fiscal impact on either the State as a whole or on a segment of the State.

Generally, the statewide concerns that follow fall into two main categories by subject: problems with financial reporting and problems with compliance with state or federal requirements. Included in the problems with financial reporting are the following issues:

- Failure to document differences in accounting practices used by the State Controller's Office and the Department of Finance;
- Problems with the State's conversion of its accounting policies to generally accepted accounting principles; and
- Failure to require departments to submit important financial reports to the State Controller's Office to improve the reliability of the State's general purpose financial statements.

Included in the weaknesses in compliance with federal and state policies are the following:

- Accumulation of potentially excessive revenues in internal service funds, resulting in a possible liability to the federal government for overcharges;
- Reduction of anticipated salary savings available to the State's General Fund;
- Lack of monitoring of recipients of federal and state moneys, resulting in the State's inability to ensure that the moneys are being used appropriately;

- Inability to track expenditures of federal moneys for each federal program; and
- Lack of compliance with the state and federal requirements for the drug-free workplace.

Many of the statewide concerns have been reported by the Bureau of State Audits for fiscal year 1991-92 and by the Office of the Auditor General for prior years. Some of the statewide concerns remain unresolved because they require the coordinated efforts of many agencies or require the expenditure of scarce resources. Four issues are reported as a statewide concern for the first time this year: the widespread inadequacies with monitoring of recipients of state and federal moneys, the lack of procedures to ensure compliance with the drug-free workplace requirements, the reduced availability to the State's General Fund of anticipated salary savings, and the absence of a comprehensive, centralized record of federal receipts for the State.

Potential Liability to the Federal Government for Some Internal Service Funds

The State may have a liability to the federal government estimated to be as much as \$19.7 million for profits accumulated in certain internal service funds between July 1, 1984, and June 30, 1993. This condition exists because the Department of Finance has not ensured that charges to federal programs are in compliance with federal regulations. The State's internal service funds provide goods and services to state agencies and charge them for these goods and services. In turn, the state agencies have passed these charges on to federal programs that the State administers. When the charges of internal service funds exceed the costs for providing services, the State accumulates profits in its internal service funds.

In 1984, the federal Department of Health and Human Services (DHHS) audited the State's rate-setting methods for internal service funds. As a result of the audit, the State was required to refund to the federal government approximately \$14.9 million of the profits accumulated in its internal service funds. This amount represented the federal share of profits accumulated by five of the State's internal service funds from July 1, 1969, to June 30, 1984. Because some of these internal service funds continue to accumulate profits, the State may be liable to the federal government for the portion of the additional surplus accumulated between July 1, 1984, and June 30, 1993, that represents charges to federal programs.

Currently, the federal DHHS is conducting an audit of the State's rate-setting methods for internal service funds for the period July 1, 1984, through June 30, 1991. As of April 30, 1994, the DHHS had not issued its final report.

Because we did not have the DHHS's final report, we estimated the liability. We used procedures similar to those of the Department of Finance, employing the same percentages used to determine the federal share of the State's profits in the 1984 audit for four of the five internal service funds that the DHHS audited and a revised percentage for the other. Using these procedures, we estimate that, under current federal regulations, the State may owe the federal government as much as \$19.7 million. This amount is the federal share of profits accumulated by four of these funds from July 1, 1984, through June 30, 1993, less audit adjustments and undercharges to federal programs of approximately \$507,000 for one fund. Because the federal government and the State's executive branch are ultimately responsible for negotiating any final settlement, we did not attempt to determine whether the earlier percentages we used for the federal portion of the profits are acceptable for the period from July 1, 1984, through June 30, 1993. Also, we did not verify the accuracy of the revised percentage used in the calculation of the federal share of profits for the remaining fund.

In addition, an October 1988 amendment to the federal Office of Management and Budget (OMB) Circular A-87, *Cost Principles for State and Local Governments*, which has been proposed but not yet approved, would allow state agencies a reasonable working capital reserve of 60 days' cash expenditures. If approved, this amendment may reduce the estimated liability for three of these funds to approximately \$8.7 million. The remaining two funds have not accumulated a working capital reserve of 60 days' cash expenditures. The federal DHHS Division of Cost Allocation has temporarily authorized a request from the State of Oregon to retain a 60-day working capital reserve even though the revisions to OMB Circular A-87 have not been finalized. In January 1994, the State of California requested a similar authorization to retain a working capital reserve of 60 days' worth of cash expenditures. However, according to correspondence dated May 6, 1994, the DHHS's Division of Cost Allocation will not respond to the State's request until the current federal audit is completed.

While the State's internal service funds may be in compliance with state laws that allow them to accumulate surpluses up to certain limits, they may not be in compliance with the current provision of the OMB's Circular A-87. This circular does not allow the State to charge federal programs for amounts that exceed costs. The California Government Code, Section 13070, provides the Department of Finance with general powers of supervision over all matters concerning the financial and business policies of the State. Therefore, it is the responsibility of the Department of Finance to provide adequate guidelines to the agencies that administer internal service funds to ensure that charges to federal programs are in compliance with those federal programs.

Use of Anticipated Salary Savings

The Department of Finance (DOF) allowed certain departments to use funds that would have been available for future General Fund expenditures. As a result, the State has approximately \$16.5 million less for future General Fund expenditures than originally anticipated. In addition, these departments were afforded a benefit not provided to other General Fund departments.

Chapter 83, Statutes of 1991, eliminated two special accounts in the Public Employees' Retirement System (PERS). The balances in these accounts are being used to offset the employer contributions to the PERS for General Fund departments. The salary savings resulting from the reduction of General Fund retirement contributions would be available for future General Fund expenditures. However, when the State Controller's Office (controller) sought to collect the salary savings, many departments did not have appropriation balances sufficient to cover their share of the savings. Most departments were then asked to adjust their spending to provide sufficient funds for the controller to ultimately collect the savings. However, the DOF allowed the Department of Industrial Relations (DIR), the California Youth Authority, and the California Department of Forestry to remit less than their respective shares of the savings.

For example, the DOF effectively allowed the use of approximately \$1.9 million of the salary savings to support the DIR's operations. The DIR would have overspent its 1991-92 support appropriation by approximately \$1.9 million if the controller had collected the DIR's share of the salary savings. The DIR sought approval from the DOF for the creation of deficiency funding to enable the return of the savings to the General Fund surplus. In accordance with the California Government Code, Section 11006, and Section 27 of the annual Budget Act, the DOF has authority to approve the creation of a deficiency in an appropriation, when necessary, provided that the Legislature is notified

at least 30 days before the effective date of the approval. However, the DOF did not believe a deficiency could be supported and recommended that nothing be done to fund the return of the savings to the General Fund surplus. This effectively resulted in the use of the salary savings to support the DIR's operations.

As a result of these actions, the State did not realize approximately \$16.5 million in anticipated salary savings that would have been available for appropriation by the Legislature. In addition, the DOF, in effect, allowed the DIR to circumvent normal budgetary controls by recommending that the DIR do nothing to fund the return of the salary savings to the General Fund surplus. Further, the reductions of department appropriations related to the salary savings were not consistently applied. Therefore, some departments benefited because they were not required to return their full share to the General Fund surplus.

Lack of Documentation of Differences in Accounting Practices

The State Controller's Office (controller) and the Department of Finance (DOF) each report on the State's budgetary basis financial condition using different accounting practices, but neither agency is able to provide us with documentation clearly identifying all the differences. For example, we do not have documentation of the reasons for the following differences. For fiscal year 1990-91, the controller reported a General Fund deficit of \$1.3 billion in its Annual Report and the DOF reported a General Fund deficit of \$920 million in the Governor's Budget, resulting in a \$400 million difference for the same reporting period. These differences in the reporting of the State's budgetary basis financial condition continue to exist. For example, the controller reported the General Fund deficit for fiscal year 1991-92 at \$3.31 billion, more than \$1 billion greater than the \$2.29 billion deficit reported by the DOF for the same reporting period. In addition, the controller reported the General Fund deficit for fiscal year 1992-93 at approximately \$2.24 billion, which was approximately \$50 million less than the \$2.29 billion deficit reported by the DOF for the same reporting period. However, the DOF has indicated that its financial information for fiscal year 1992-93 may change.

Inconsistent accounting practices and the lack of documentation of those differences provide the State's financial decision makers and the investment community with conflicting information about the State's true financial condition. For example, the State Treasurer's Office has to disclose in its prospectus for the sale of state bonds that the controller and the DOF use different accounting practices. The disclosure is necessary because schedules prepared by the two

Problems With the State's Conversion to GAAP

organizations are included in the prospectus, but the schedules do not agree with each other. In addition, because the DOF's records are used in the State's budgeting process, the lack of documentation of differences in accounting practices may impair the integrity of the budgeting process.

The State prepares financial statements on a budgetary basis and on a basis consistent with generally accepted accounting principles (GAAP). The State Controller's Office (controller) currently issues the Annual Report of the State of California in general conformity with the State's budgetary basis of accounting, which is not in accordance with GAAP. The State's budgetary statements must then be converted to GAAP for the State's general purpose financial statements. The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness during its audits for fiscal years 1982-83 through 1990-91.

The budgetary basis financial statements are required by the California Government Code, Section 12460, which states that the controller will prepare an annual report containing a statement of the funds of the State, its revenues, and the public expenditures of the preceding fiscal year on the same basis as that of the governor's budget and the budget act. This section also requires that the format of the budgetary report be prepared as closely as possible in accordance with GAAP. GAAP is the preferred method of accounting because it is a nationally recognized set of accounting principles that improve accountability, recognizing costs when they occur, not when they are paid.

Nevertheless, significant differences exist between the budgetary basis and GAAP basis financial statements, requiring adjustments to present financial statements in accordance with GAAP. The adjustments are necessary because the following budgetary accounting practices for the State's General Fund are not in accordance with GAAP:

- Expenditures such as the cost of earned vacation for certain state faculty are not recognized;
- If an appropriation has no remaining funds, the liabilities are not recognized; and

- Some events are recognized as expenditures even though no cost has been incurred. For example, the State reports loans from the General Fund to other funds as expenditures, rather than recognizing that the money was lent to another fund and will be returned to the General Fund.

Adjustments are also necessary to present the fund balances of the State's other fund types (as reported by the controller) in accordance with GAAP because of the following budgetary accounting practices followed by the State:

- The State recognizes its authorized but unissued bonds as an addition to fund balance. Under GAAP, the proceeds from the sale of bonds should not be recognized until the sale occurs;
- The State reports as encumbrances grants to local agencies when the commitments are made. Under GAAP, the grants are not reported as encumbrances because the local agencies, not the State, receive the related goods or services. Instead, under GAAP, these encumbrances are reported in the notes to the financial statements as commitments;
- The State does not consistently recognize expenses such as the cost of earned vacation and worker's compensation claims in its funds, as required by GAAP. If audit adjustments for these expenses were not made in the internal service funds, the State's possible liability to the federal government, described on page 6, would be increased by approximately \$5.7 million; and
- At least one internal service fund includes encumbrances in its liability balance because the State Administrative Manual does not provide adequate direction for the accounting for internal service funds. Under GAAP, encumbrances are not reported as liabilities.

In addition, the financial information required under GAAP is more extensive than the information provided by the budgetary basis of accounting. As a result, the State must develop additional information for proprietary funds, lease commitments, and the market value of the State's investments in securities to create its general purpose financial statements.

A primary reason these differences exist is the failure of the Department of Finance (DOF) to provide agencies with sufficient instruction in the State Administrative Manual to make the conversion

from the budgetary basis to GAAP efficient and reliable. As a result, the financial information that agencies provide to the controller is frequently insufficient for the controller to prepare the State's general purpose financial statements in accordance with GAAP.

However, the State is in the process of converting from the budgetary basis to GAAP in certain areas. The DOF has rewritten some sections of the State Administrative Manual covering proprietary funds to bring them into conformity with GAAP under certain conditions. In addition, in the governor's budget, the DOF currently treats the State's General Fund encumbrances as a reservation of fund balance rather than as expenditures and has extended this treatment to the year-end financial statements. This treatment changes earlier practices and is consistent with GAAP, in that encumbrances are obligations for which goods and services have not been received, and they should not be shown as expenditures. Additionally, in accordance with GAAP, the State now recognizes in its financial statements the liability for Medi-Cal services provided but not yet paid for and the liability for tax overpayments. However, until the State incorporates all of the necessary generally accepted accounting principles into state law, the State must continue spending time and money to convert its financial records from the budgetary basis to GAAP so that the financial statements are comparable to those of other governmental entities and, therefore, acceptable to the investment community and the federal government under the single audit act.

Inadequate Monitoring of Recipients of State and Federal Moneys

The State is often deficient in its monitoring of recipients of state and federal moneys. We found the administration of 19 federal programs in 8 departments deficient in a wide variety of required monitoring practices. These deficiencies include failure to conduct audits or reviews of recipients' operations or records, to ensure the receipt of audit reports completed by independent auditors on recipient operations, and to monitor recipient cash balances. The table beginning on page 199 lists the federal programs for which we found such deficiencies. We found the following examples of deficient monitoring:

- The Department of Aging did not conduct required, annual on-site performance evaluations of supportive services for 17 of 33 area agencies or similar biennial evaluations of nutrition services for 20 of 33 area agencies for the Special Programs for the Aging—Title III.

- For 19 of 52 recipients of Job Training Partnership Act funds, the Employment Development Department did not enforce its requirement that recipients maintain interest-bearing accounts. As a result, the State could lose potential interest earnings.
- The Department of Health Services failed to conduct required biennial site visits for the Special Supplemental Food Program for Women, Infants, and Children at 26 of 80 local agencies.
- According to its records on close-out audits of school construction projects funded by state bond moneys, the Office of Local Assistance had 1,200 construction projects that were ready for audit, 204 of which had been ready for more than four years.
- The California Department of Education had numerous weaknesses in its monitoring of local educational agencies participating in the Eisenhower Mathematics and Science Education—State Grants program. The weaknesses included inadequate control over expenditure reports from local educational agencies and insufficient monitoring to ensure that children and teachers from private, nonprofit schools had equitable participation in the program.
- Ten of the 54 counties participating in the Alcohol and Drug Abuse and Mental Health Services Block Grant administered by the Department of Mental Health failed to submit a final cost report to the department, limiting the department's ability to monitor the expenditure of federal block grant funds. In addition, quarterly reports from four of the ten counties we reviewed indicated that the counties had cash balances of block grant moneys that exceeded their immediate needs.
- Five of the 16 Community Based Organizations participating in the Job Training Partnership Act program administered by the California Department of Education failed to submit required audit reports more than 17 months after they were due. In addition, even though the reports that were received identified control deficiencies, the department did not send any of its own required reports, called "Initial Determinations," intended to help correct deficiencies. The Initial Determinations, which are to be sent within 30 days, had not been sent more than 17 months after the audit reports were due.

Without adequate monitoring of recipients of state and federal moneys, the State cannot ensure the recipients are complying with regulations or laws governing the receipt or use of these moneys.

Inadequate Reporting of Leasing Information

The State does not have centralized records that contain all the necessary information for financial statement disclosures on lease commitments required by GAAP. Without centralized records, the State spends unnecessary time and effort in gathering and summarizing the required information. The State's lease commitments totaled approximately \$5.8 billion in fiscal year 1992-93, excluding leases between the University of California and nonstate entities.

Governmental accounting and reporting standards require that governmental accounting systems allow the fair presentation and full disclosure of the governmental entity's financial position and results of financial operations in accordance with GAAP. In addition, the California Government Code, Section 12460, requires the State Controller's Office to present the State's financial position in a format that is as close as possible to GAAP. When the State leases space or equipment from outside vendors, GAAP requires the State to disclose commitments for future minimum lease and rental payments in a summary that separates these future payments by fiscal year.

Although the Department of General Services maintains space and equipment records for many lease commitments, it established these records for its internal management purposes, rather than for maintaining a complete listing of the State's leases that would meet GAAP requirements. As a result, the records do not provide all the required information. For example, the records disclose only the current-year payments for each lease and do not indicate either the changes in the payments in future years or the separate future lease and rental payments by fiscal year.

The records also do not include information on certain leases for which the Department of General Services does not have oversight responsibility. For example, the department's records do not include more than \$1.7 billion in lease commitments with the State Public Works Board or \$8.2 million in lease commitments for the California State Lottery Commission.

The Bureau of State Audits reported this weakness in its audit for fiscal year 1991-92, and the Office of the Auditor General reported the weakness for fiscal years 1986-87 through 1990-91.

Confusion Over Requirements for Approval for Some Contracts

The State Administrative Manual does not provide adequate guidance about which agreements for services are grants and which are contracts requiring the approval of the Department of General Services (DGS). The Public Contract Code, Section 10295, states that all contracts entered into by any state agency for services are void unless and until approved by DGS. In addition, the Health and Safety Code, Section 38012, requires DGS's approval of direct service contracts entered into by departments in the Health and Welfare Agency. The Attorney General's Office has issued two opinions that precede the effective date of the direct service contract legislation, one in 1975 and one in April 1980. The opinions distinguish grants from contracts, and they state that certain grants are not contracts for services and are, therefore, not subject to DGS's review and approval.

Some departments have relied on the opinions of the Attorney General's Office as their rationale for not obtaining DGS's approval of agreements for services. For example, the Office of the Auditor General reported in 1989 that the Department of Aging and the Department of Health Services did not always obtain DGS's approval of contracts when it was required. The departments, both of which are in the Health and Welfare Agency, responded that they considered the contracts in question to be grants, basing their positions on the opinions of 1975 and 1980. However, a more recent opinion of the Legislative Counsel, obtained during the Office of the Auditor General's audit, determined that some of these contracts did not meet the legal definition of a grant.

In our current review of similar or identical contracts at these two departments, we found that the Department of Health Services continues to cite the opinions of the Attorney General's Office in classifying an Indian Health Program contract as a grant, even though the Legislative Counsel concluded that the agreement in question was a direct service contract and, therefore, subject to DGS's review and approval. During fiscal year 1992-93, the Department of Health Services entered into agreements totaling \$2.3 million for the Indian Health Program. In contrast to the response of the Department of Health Services to the 1989 audit, the Department of Aging reviewed its contracts to determine if they met the legal definition of a grant. The Department of Aging concluded that many contracts that it had previously classified as grants were actually contracts subject to DGS's review and approval.

DGS provides an independent review of contracts to ensure that state agencies are complying with laws and regulations and that the financial interests of the State are preserved and protected. If a department

incorrectly classifies a contract as a grant, the State's system of controls is circumvented, and the State has less assurance that its financial interests are being protected.

The DGS should solicit a current opinion from the Attorney General's Office that clearly identifies the factors distinguishing grants from contracts and that clearly identifies when an agreement is subject to DGS's review and approval. DGS should then ensure that the State Administrative Manual accurately provides this information.

Deficiencies in Administering State Contracts

State agencies do not consistently comply with the California Public Contract Code in establishing and reviewing contracts. During fiscal year 1992-93, work began on some contracts before the contracts were approved. In addition, the Department of General Services (DGS) frequently fails to conduct required audits of state agencies to which purchasing authority has been delegated.

In our review of 85 nonconsultant contracts at 17 departments, we found 13 contracts (15 percent) that were not approved before the beginning of contract work. When agencies do not ensure that contracts are approved before work begins, the State cannot be assured that its interests are protected. Further, if these contracts had not been subsequently approved, the State might still have been liable for the work performed and might have incurred litigation costs regarding the State's obligation to pay for that work. The Bureau of State Audits reported this weakness for fiscal year 1991-92, and the Office of the Auditor General reported this same problem for fiscal years 1986-87 through 1990-91.

Table 1 below indicates the departments at which we reviewed nonconsultant contracts, the number of contracts reviewed, and the number of contracts reviewed for which work began before contract approval. The table pertains specifically to our review of nonconsultant contracts. We released a report in April 1994 that addresses our review of consultant contracts for fiscal years 1991-92 and 1992-93.

**Table 1 Deficiency in Administering State
Nonconsultant Contracts at Various Agencies
Fiscal Year 1992-93**

Agency Name	Contracts Tested	Contracts That Lacked Approval Before Start of Work
Department of Health Services	5	4
California Department of Education	5	3
Stephen P. Teale Data Center	5	2
Health and Welfare Agency Data Center	5	1
State Treasurer's Office	5	1
Department of General Services	5	1
Department of Transportation	5	1
Department of Motor Vehicles	5	0
Department of Social Services	5	0
Franchise Tax Board	5	0
Department of Water Resources	5	0
California Community Colleges, Chancellor's Office	5	0
State Controller's Office	5	0
Department of Corrections	5	0
Employment Development Department	5	0
Board of Equalization	5	0
California State University, Office of the Chancellor	5	0
Total	85	13

The California Public Contract Code, Section 10295, states that all contracts, unless otherwise exempt, entered into by any state agency for the purchase of equipment, supplies, materials, services, or construction are void unless or until approved by DGS. In addition, Section 10335 states that, unless specifically exempted, a service contract is not effective until the date of its approval. Moreover, the State Administrative Manual, Section 1209, requires state agencies to submit each contract in sufficient time for DGS to review and comment on it before work on the contract begins, except in emergency cases to protect human life or state property. This section of the manual also states that a contractor who begins work before receiving notice of the contract's approval may be considered to have performed the work at the contractor's own risk and may not be paid. When contracts are exempt from DGS's approval, the issuing department should approve the contract before work begins.

In another departure from control procedures over the State's contracting process, DGS frequently fails to conduct required audits. The Public Contract Code, Section 10333(b), requires DGS to audit each state agency to which the department has delegated purchasing authority at least once every three years. As of August 6, 1993, DGS delegated purchasing authority valued at more than \$214 million to 151 departments. However, it had not audited 80 of these departments within the required three years. As a result, DGS cannot ensure that almost \$99 million in delegated purchasing authority is properly managed and controlled.

Failure To Require Agencies To Prepare Reconciliations or Reports of Accruals

At the end of each fiscal year, state agencies submit financial reports to the State Controller's Office (controller), which then issues a combined financial report presenting the State's financial position and results of operations. However, the State Administrative Manual, Section 7951, does not require agencies to submit to the controller two important financial reports for more than 225 funds numbered 500 to 699 and 800 to 999. We found the following:

- Report 15, Reconciliation of Agency Accounts With Transactions Per State Controller, is not submitted. As a result, the controller does not have evidence that agencies have reconciled financial information that appears in the general purpose financial statements with records of the controller. The State Administrative Manual, Section 7900, discusses the importance of making regular reconciliations. Reconciliations represent an important element of internal control because they provide a high level of confidence that transactions have been processed properly and that the financial records are complete. The reconciliation with the records of the controller is an important step in ensuring the accuracy of the agencies' financial statements.
- Report 1, Report of Accruals to the Controller's Accounts, also is not submitted. As a result, information needed to distinguish encumbrances from accounts payable and to present financial information in accordance with GAAP is not available for all funds. The California Government Code, Section 12460, requires the controller to present the State's financial position in a format that is as close as possible to GAAP. In addition, Section 1100.101 of the *Governmental Accounting and Financial Reporting Standards*, issued by the Governmental Accounting Standards Board, requires

that agencies' accounting systems make it possible to present fairly the agencies' financial positions and results of operations in accordance with GAAP.

Included among these funds are more than 70 that had budget appropriations for fiscal year 1992-93. Without the reconciliation and accrual information for these funds, the controller cannot be assured that expenditures for these funds are within the budgeted limits. The Bureau of State Audits reported similar weaknesses for fiscal year 1991-92, and the Office of the Auditor General reported similar weaknesses for the previous six fiscal years.

Ineligibility for Certificate of Achievement

The State does not yet qualify for the Certificate of Achievement for Excellence in Financial Reporting. The Certificate of Achievement Program of the Government Finance Officers Association encourages and recognizes excellence in financial reporting by governments. The State does not qualify for the certificate primarily for the following two reasons:

Late Audited Financial Statements

The State has not been able to produce the necessary financial reports in time to issue audited financial statements within six months of the end of the fiscal year, a time requirement established in 1980 by the Government Finance Officers Association. While major corporations such as IBM, General Motors, and Pacific Gas and Electric are required to issue their audited financial statements within 90 days after the close of the fiscal year, the State is allowed 180 days. However, the State has repeatedly taken longer than 200 days to issue its audited financial statements. The report on the financial statements for fiscal year 1992-93 was dated April 30, 1994, more than 300 days after the fiscal year ended.

To address this concern, the Office of the Auditor General contracted with Price Waterhouse to evaluate the State's financial reporting system. In its report, issued in May 1987, Price Waterhouse identified shortcomings throughout the State's financial reporting system and made recommendations for correcting them. In response to Price Waterhouse's recommendations, the State formed a committee consisting of representatives from various control agencies to improve the State's reporting system. The committee has initiated a pilot project to make financial reporting more accurate and prompt. The project involves the development of the following:

- automated reconciliations of agency records with the controller's records;
- a proposed reduction in the number of reports required from agencies; and
- a preliminary plan for electronic reporting of year-end financial data to the controller.

Lack of Combining Statements by Fund Type

The State has not included combining statements by fund type in its audited financial statements. These combining statements provide financial statements of each of the individual funds within the fund types shown in the general purpose financial statements. Section 2200.101 of the *Governmental Accounting and Financial Reporting Standards*, issued by the Governmental Accounting Standards Board, states that every governmental unit should prepare a Comprehensive Annual Financial Report that includes general purpose financial statements by fund type and account group as well as the combining statements by fund type and individual fund statements.

The State has not prepared combining statements by fund type in accordance with these guidelines issued by the Governmental Accounting Standards Board. The State's system accounts for its funds in a manner that, in some cases, is not in full agreement with GAAP. For example, the State accounts for some of its funds in the Trust and Agency fund type and Capital Project fund type on the budgetary basis, but reports the same funds in the Special Revenue fund type in the general purpose financial statements.

However, the State has made progress toward preparing combining statements by fund type. Specifically, the State is in the process of organizing the funds within each fund type into categories that have a similar purpose for presentation in the Comprehensive Annual Financial Report. In addition, the State is modifying its automated system that produces the financial statements. The system will summarize the budgetary basis statements into GAAP classifications for presentation in the Comprehensive Annual Financial Report.

The Bureau of State Audits reported a similar weakness during its audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness during its audits for the previous six fiscal years.

Inability To Account for Expenditures of Federal Money by Each Federal Program

The State is not in compliance with a requirement of OMB Circular A-128 to present a schedule of federal assistance that shows total expenditures for each federal assistance program. The State cannot comply because it does not record its expenditures by federal program. The schedule of federal assistance that we present, beginning on page 175, shows total receipts by program, rather than expenditures.

The OMB's Circular A-128 requires the State to submit an audit report on a schedule of federal assistance that shows the total expenditures for each federal assistance program. The California Government Code, Section 13300, assigns the Department of Finance the responsibility for establishing and supervising a complete accounting system to ensure that all revenues, expenditures, receipts, disbursements, resources, obligations, and property of the State are properly accounted for and reported.

The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness during the audits for fiscal years 1985-86 through 1990-91. The Department of Finance has reported that making the necessary modifications to the State's automated systems would require extensive effort.

Lack of Centralized Records for Federal Receipts

The State does not have centralized records for recording the receipt of federal moneys, potentially resulting in an impairment of the State's ability to satisfy federal requirements for the continued receipt of federal moneys. The federal OMB Circular A-128 identifies these requirements. Specifically, it requires the State to prepare and render an opinion annually on a schedule of federal assistance. In addition, the circular requires the State to identify all federal grants from which the State receives more than \$20 million in a single year and ensure that the grants are audited for that year.

In 1978, the State took steps to establish a centralized record of federal receipts. In that year, the State created the Federal Trust Fund for the deposit of all moneys received by the State from the federal government where the expenditure was administered through or under the direction of any state agency. The purpose in creating the fund was to provide better accountability for the State's receipts and expenditures of federal funds. If the State consistently required all federal receipts to be recorded in the Federal Trust Fund, the centralized records to help satisfy requirements under Circular A-128 would exist.

However, the State has allowed exceptions to the rule that all federal receipts are to be recorded in the Federal Trust Fund. For example, Section 89725 of the Education Code, which was established by statute in 1991, allows the Federal Trust Fund to be bypassed for receipts for student financial aid at the California State University. During fiscal year 1992-93, these receipts totalled almost \$140 million. In addition, the Department of Finance administratively created the State Legalization Impact Assistance Fund to account for receipts and expenditures from the federal State Legalization Impact Assistance Grants. These receipts totaled more than \$1.4 billion for fiscal years 1988-89 through 1992-93.

The absence of the centralized records results in additional work to prepare the schedule of federal assistance required by Circular A-128. For example, to determine fiscal year 1992-93 receipts to include in the schedule, the State had to request that the California State University separately identify receipts for each of the student financial aid grants. In addition, the potential exists that the State will fail to identify all receipts. This lack of identification could result in material misstatements in the schedule of federal assistance or the failure to identify all grants requiring an audit under Circular A-128.

Lack of Compliance With Drug-Free Workplace Requirements

Many departments do not comply with state and federal drug-free workplace requirements. To comply with the federal Drug-Free Workplace Act of 1988 and to continue receiving federal grants and contracts, the State must certify that it provides a drug-free workplace. In 1989, the State took steps to comply with the requirements of the federal legislation. In a management memorandum, dated April 14, 1989, the Department of Personnel Administration directed departments to provide to their employees a copy of the State's formal drug-free workplace statement. The statement complies with the federal requirements by disclosing the State's policy on the drug-free workplace; indicating the penalties for violations of the policy; and providing notification of the availability of assessment, counseling, and rehabilitation services through the State Employee Assistance Program. Further, the Government Code, Section 8355, requires any contractor with the State to publish a similar statement of notification to the contractor's employees. The State Administrative Manual, Section 1253, further clarifies contracting requirements for the Drug-Free Workplace Act.

Despite the extensive sources of information about the requirements, we found that state departments often do not fully comply with the drug-free workplace procedures. Six departments that we reviewed for

compliance with contracting procedures lacked drug-free workplace certificates for some of the contracts we examined. In addition, for the departments at which we reviewed internal controls for selected federal programs, seven departments either had no procedures in place for ensuring a drug-free workplace or had inadequate procedures. For example, the Office of Statewide Health Planning and Development and the Emergency Medical Services Authority do not have continuing policies for ensuring their employees are aware of the requirements of the Drug-Free Workplace Act. Without such programs, the departments cannot ensure their employees are aware of the drug-free workplace policy and any assistance available to them.

**Salary Warrants
Are Not Always
Promptly
Returned**

State departments do not always return undelivered salary warrants to the State Controller's Office within 90 calendar days of receipt. We performed tests for undelivered salary warrants more than 90 days old at 40 locations and found that, at 21 locations, department staff did not return a total of 388 salary warrants to the State Controller's Office within 90 days of receipt. These warrants ranged in amount from \$0.68 to \$10,658.44. The oldest warrant found was written more than 8 years ago. Although failure to return the undelivered warrants to the State Controller's Office does not cause any financial harm to the State, it increases the risk of their loss or misappropriation. The following table provides, by department, the number of undelivered salary warrants that were more than 90 days old.

**Table 2 Salary Warrants Not Returned
Within 90 Days**

Agency	Number of Warrants More Than 90 Days Old	Amount of Warrants
California Conservation Corps	50	\$ 11,363.00
California State University (Four campuses)	106	36,133.51
Corrections, Department of (Five institutions)	36	11,947.74
Developmental Services, Department of (Four developmental centers)	27	8,715.21
Mental Health, Department of (One hospital)	52	9,903.17
Motor Vehicles, Department of	99	29,257.36
Parks and Recreation, Department of	3	11,404.32
Rehabilitation, Department of	3	3,189.32
Toxic Substances Control, Department of	9	1,873.65
Transportation, Department of (Two districts)	3	189.28
Total	388	\$ 123,976.56

The State Administrative Manual, Section 8580.5, requires that salary warrants not delivered within 90 calendar days of receipt must be returned to the State Controller's Office for monthly deposit in the special deposit fund.

**Improper
Omissions From
the State
Reporting Process**

District Agricultural Associations, which are organized to hold fairs and expositions, are not treated as part of the State's financial reporting entity. To determine whether the financial information of the District Agricultural Associations should be included with the State's general purpose financial statements, we requested a legal opinion from the Legislative Counsel. The Legislative Counsel found that the District Agricultural Associations are state agencies and that money they spend is state money. Further, funds for the support of the District Agricultural Associations are appropriated in the State's annual budget. For these reasons, the Legislative Counsel concluded that the State Controller's Office is required to include the financial information of the District Agricultural Associations in the State's general purpose financial statements. Currently this information is not included, and as a result, the State's general purpose financial statements are incomplete.

The Bureau of State Audits reported a similar finding for fiscal year 1991-92, and the Office of the Auditor General reported a similar finding for fiscal years 1987-88 through 1990-91.

Audit Information by Area of Government

Summary The State of California continues to incur unnecessary costs and face the reduced efficiency and effectiveness of its operations because of weaknesses in its internal control structure. Although the State has corrected some of the problems the Bureau of State Audits reported for its audit of fiscal year 1991-92 and the Office of the Auditor General reported for audits of prior years, the State can still significantly improve its accounting and administrative controls.

Table 3 below summarizes state expenditures and the financial and compliance audit activity of the Bureau of State Audits during fiscal year 1992-93. Other audits issued by the Bureau of State Audits and the former Office of the Auditor General are also summarized in the final column of the table and cover the period from July 1, 1992, through December 31, 1993. The table organizes this information according to the nine areas of government recognized in the Governor's Budget for fiscal year 1992-93. The Bureau of State Audits conducted financial and compliance audit work in each of the nine areas of government. Two areas of government, the Health and Welfare area and Education area, have significant expenditures, totaling more than 75 percent of the State's expenditures, and receive moneys from 38 major federal grant programs. The Bureau of State Audits conducted extensive financial and compliance audit work in the departments in these two areas of government.

Table 3
Summary of Audit Work by Area of Government

Area of Government	Total Amount/ Percent of State Expenditures*	Number of Departments				Number of Special Topic Reports
		In Area of Government	Audited*	With Reported Weaknesses	Amount/Number of Federal Grants Audited	
Business, Transportation and Housing	\$6.9 billion 6.2%	18	\$5.9 billion 5	4	\$1.314 billion 2	2
Education	\$44.6 billion 39.6%	16	\$30.8 billion 5	4	\$2.161 billion 15	3
Environmental Protection	\$6 billion .5%	6	\$3 billion 1	0	\$0.097 billion 2	1
General Government	\$7.5 billion 6.7%	54	\$4 billion 4	4	\$1.157 billion 4	2
Health and Welfare	\$46.8 billion 37.1%	20	\$39.3 billion 10	7	\$15.366 billion 27	4
Legislative, Judicial and Executive	\$2.1 billion 1.8%	39	\$8 billion 5	1	\$2.227 billion 4	3
Resources	\$2.0 billion 1.8%	23	\$9 billion 3	0	0	1
State and Consumer Services	\$3.8 billion 3.4%	13	\$7 billion 3	2	0	1
Youth and Adult Correctional	\$3.2 billion 2.9%	6	\$3.2 billion 3	1	\$0.007 billion 2	1

* Amounts reported in these columns are total estimated expenditures for all state departments in the agency or for all departments audited during fiscal year 1992-93. Estimated amounts are from the Governor's Budget for fiscal year 1994-95. The estimates do not reflect actual amounts audited.

Table 4, which begins on page 30, summarizes the results of the financial and compliance audit work that the Bureau of State Audits conducted for fiscal year 1992-93. The Bureau of State Audits reports the results of these audits in management letters addressed to the administrators of each of the departments with audit issues to report. These management letters are included in this report, beginning on page 39.

Table 4 shows the distribution by state department of weaknesses in control over financial activities and weaknesses in compliance with state and federal regulations. The page number column in the table provides the location in this report of the beginning of the specific management letter for the indicated state department. The numbers in the other columns are the item numbers for each weakness reported in the management letters for the departments. A more detailed table describing the type of weaknesses found in compliance with federal regulations begins on page 199.

TABLE 4**WEAKNESSES IN INTERNAL CONTROL SYSTEMS**

Agency	Page Number	Weaknesses and Item Numbers ^a					
		Financial Reporting Activities	Revenue Activities/ Safeguarding of Assets	Expenditure and Electronic Data Processing Activities	Compliance With Federal Activities	Compliance With State Regulations ^b	Compliance With State Regulations
BUSINESS, TRANSPORTATION AND HOUSING							
Housing and Community Development, Department of	47			1	1 - 6		1,4,6
Motor Vehicles, Department of	51			1 - 2		1 - 2	
Stephen P. Teale Data Center	53	1,3	4		2	1 - 4	
Transportation, Department of	59	4	1		2 - 3	1,4	
EDUCATION							
California Community Colleges, Chancellor's Office	67					1	
California Postsecondary Education Commission	68		3			1-2,4-5	3
California Student Aid Commission	72					1 - 6	5
Education, California Department of	78		12			1-11,13-14	1,6,12

Footnotes are presented on page 32.

Agency	Page Number	Weaknesses and Item Numbers ^a				
		Financial Reporting Activities	Revenue Activities/ Safeguarding of Assets	Expenditure and Electronic Data Processing Activities	Compliance With Federal Regulations ^b	Compliance With State Regulations
GENERAL GOVERNMENT						
Criminal Justice Planning, Office of	97			1 - 9	7	
Economic Opportunity, Department of	103				1	
Finance, Department of	105				1	
Military Department	109		1			
HEALTH AND WELFARE						
Aging, Department of	113			1-2		
Alcohol and Drug Programs, Department of	115			1 - 3	1	
Employment Development Department	118			1-5	6	
Health and Welfare Agency Data Center	124			1	1	
Health Services, Department of	127	1	3,10	2,4-10	1,3,10	
Mental Health, Department of	138				1 - 3	
Social Services, Department of	141				1 - 3	
LEGISLATIVE, JUDICIAL, AND EXECUTIVE						
Emergency Services, Office of	147			1 - 3	1	

Footnotes are presented on page 32.

Agency	Page Number	Weaknesses and Item Numbers ^a					
		Financial Reporting Activities	Revenue Activities/ Safeguarding of Assets	Expenditure and Data Processing Activities	Electronic Data Activities	Compliance With Federal Regulations ^b	Compliance With State Regulations
STATE AND CONSUMER SERVICES							
California Museum of Science and Industry	151			1 - 2		1 - 2	
General Services, Department of	154	3 - 4			1	1 - 6	
YOUTH AND ADULT CORRECTIONAL							
Youth Authority, Department of the	163			1 - 2			

^aThe item number is the number of each weakness as presented in the report on each state agency.

^bThe table on page 199 provides more detail regarding the weaknesses in compliance with federal regulations.

Report on the Internal Control Structure



CALIFORNIA STATE AUDITOR

BUREAU OF STATE AUDITS

KURT R. SJOBERG
State Auditor

MARIANNE P. EVASHENK
Chief Deputy State Auditor

Independent Auditors' Report on the Internal Control Structure

The Governor and Legislature of
the State of California

We have audited the general purpose financial statements of the State of California as of and for the year ended June 30, 1993, and have issued our report thereon dated April 30, 1994. We did not audit the financial statements of the pension trust funds, which reflect total assets constituting 78 percent of the fiduciary funds. We also did not audit the financial statements of certain enterprise funds, which reflect total assets and revenues constituting 92 percent and 94 percent, respectively, of the enterprise funds. In addition, we did not audit the University of California funds. The financial statements of the pension trust funds, certain enterprise funds, and the University of California funds referred to above were audited by other auditors who furnished their reports to us, and our opinion, insofar as it relates to the amounts included for the pension trust funds, certain enterprise funds, and the University of California funds, is based solely upon the reports of other independent auditors. We have also audited the State of California's compliance with requirements applicable to major federal financial assistance programs and have issued our report thereon dated April 30, 1994.

We conducted our audits in accordance with generally accepted auditing standards; *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Circular A-128, *Audits of State and Local Governments*. Those standards and OMB Circular A-128 require that we plan and perform the audit to obtain reasonable assurance about whether the general purpose financial statements are free of material misstatement and about whether the State of California complied with laws and regulations, noncompliance with which would be material to a major federal financial assistance program. In addition, we are required to review internal controls over nonmajor programs at least once during a three-year cycle.

In planning and performing our audits for the year ended June 30, 1993, we considered the internal control structure of the State of California in order to determine our auditing procedures for the purpose of expressing our opinions on the general purpose financial statements of the State of California, but not to provide assurance on the internal control structure, and on the State's compliance with requirements applicable to major federal financial assistance programs and to report on the internal control structure in accordance with OMB Circular A-128.

The State's management is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of general purpose financial statements in accordance with generally accepted accounting principles, and that federal financial assistance programs are managed in compliance with applicable laws and regulations. Because of inherent limitations in any internal control structure, errors, irregularities, or instances of noncompliance may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purpose of this report, we have classified the significant internal control structure policies and procedures in the following categories: financial activities, including electronic data processing controls; state compliance; and federal compliance. We did not study the internal control structures for the pension trust funds, certain enterprise funds, or the University of California funds.

For all of the internal control structure categories listed in the paragraph above, we obtained an understanding of the design of relevant policies and procedures and determined whether they have been placed in operation, and we assessed control risk. Because of the large number of nonmajor programs and the decentralized administration of these programs, we performed procedures to obtain an understanding of the internal control structure policies and procedures relevant to nonmajor programs on a cyclical basis. The nonmajor programs not covered during the current year are subject to such procedures at least once during the three-year cycle.

During the year ended June 30, 1993, the State of California received 97 percent of its total federal financial assistance through major federal financial assistance programs. We performed tests of controls, as required by OMB Circular A-128, to evaluate the effectiveness of the design and operation of internal control structure policies and procedures that we considered relevant to preventing or detecting material noncompliance with specific requirements, general requirements, and requirements governing claims for advances and reimbursements and amounts claimed or used for matching that are applicable to each of the State of California's major federal financial assistance programs, which are identified in the accompanying schedule of federal financial assistance. Our procedures were less in scope than would be necessary to render an opinion on these internal control structure policies and procedures. Accordingly, we do not express such an opinion.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the State's ability to record, process, summarize, and report financial data consistent with the assertions of management in the general purpose financial statements or to administer federal financial assistance programs in accordance with applicable laws and regulations.

We discuss the reportable conditions and present recommendations to correct them on pages 39 through 164 of our report. Management's comments regarding the recommendations appear on page 219 of this report. Additionally, beginning on page 207, we present a schedule listing instances of noncompliance that we consider to be minor. Specific responses to the reportable conditions identified at each state agency are on file with the Bureau of State Audits and the Department of Finance. The reportable conditions identified in the State's single audit report for fiscal year 1991-92 that have not been corrected are included in the section beginning on page 39.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the general purpose financial statements or noncompliance with laws and regulations that would be material to a federal financial assistance program may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of the internal control structure policies and procedures used in relation to the general purpose financial statements or in administering federal financial assistance would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we believe none of the reportable conditions described above is a material weakness.

In addition to the work we performed in accordance with OMB Circular A-128 and the Single Audit Act of 1984, the Office of the Auditor General performed other reviews related to federal programs. A schedule of the pertinent reports issued from July 1, 1992 to December 31, 1993, begins on page 203 of this report.

This report is intended for the information of the Governor and Legislature of the State of California and the management of the executive branch. However, this report is a matter of public record and its distribution is not limited.

BUREAU OF STATE AUDITS



SALLY L. FILLIMAN, CPA

Deputy State Auditor

April 30, 1994

Detailed Description of Weaknesses at State Agencies

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Management Letters by Area of Government

Business, Transportation and Housing

Department of Housing and Community Development

Our contractor, Pierini, Clark and Brown, reviewed the Department of Housing and Community Development's (department) administration of the U.S. Department of Housing and Urban Development grants, Federal Catalog Numbers 14.219 and 14.228.

Item 1. Failure To Follow Required Procedures for Purchase of EDP Equipment

Finding

We found an instance involving both federal and state funds in which the department's purchase of EDP equipment did not follow required state procedures. Specifically, during the tests of allowable costs and indirect cost allocations, we identified nine separate invoices under \$100,000 from a single vendor that were found to be part of a larger planned purchase of EDP equipment that was not submitted for review to the Department of General Services' Office of Procurement, as required.

The purchase requests from one division were split into two requests on the same date to keep each request below \$100,000, and personnel of the department's EDP Branch admitted to processing all requests as separate invoices for the purpose of avoiding the State's requirements on purchase orders in excess of \$100,000. Department personnel acknowledged that this planned purchase was made because excess funds were found to be available in the budget at the end of the fiscal year, and these funds would have been lost had the expenditure not been made immediately.

Criteria

Section 36 of the Common Rule states that when procuring property and services under a grant, a state must follow the same policies and procedures that it uses for procurements using nonfederal funds. The State entered into a contract with the vendor that would allow state agencies to purchase goods and services through the vendor's computer store. However, the contract specifically states that single purchases greater than \$100,000 must be forwarded to the EDP Acquisitions Unit within the Department of General Services' Office of Procurement for review.

Recommendation

Department personnel responsible for approving purchases should be reminded of the importance of adhering to existing controls, laws, and regulations. Deliberate violations of federal and state regulations raise questions about the integrity of the department and jeopardize the continued funding of certain federal programs.

Item 2. Overspending of Federal Funds for the Costs of Administering the Community Development Block Grant

Finding

For fiscal year 1991-92, the Bureau of State Audits reported that the department spent \$619,076 of federal funds in administering the Community Development Block Grants (CDBG). This amount was \$42,536 more than the \$576,540 that it was allowed to spend for this purpose. During fiscal year 1992-93, the department did not satisfactorily resolve this item. According to the department, this error occurred because expenditures were incorrectly charged to the 1991 block grant. However, 1991 block grant funds were not drawn down to cover these expenditures. The department plans to correct the mistake by transferring the expenditures to block grants from other years.

Criteria

The United States Code, Title 42, Section 5306(d)(3)(A), allows state-level expenditures for administrative costs of \$100,000 plus 2 percent of the grant amount, which for 1991-92 amounted to \$576,540.

Recommendation

The department should correct the mistake immediately.

Item 3. Inadequate Documentation To Support Requests for Transfers of Federal Funds

Finding

In testing a sample of 25 requests for transfers of federal funds, the related State Controller's Remittance Advice (RA), and the subsequent receipt of funds, we found 3 RAs did not have adequate support for either the amount of funds received or the amount of funds spent. Two RAs and subsequent receipt of funds in the amount of \$1,171,442 had documentation in claim schedules, warrants, and disbursements that supported only \$963,740 of those funds. The reconciliation of these differences was possible only through the memory, notes, and personal attention of the person responsible for these differences.

Criteria

The OMB Common Rule for Uniform Administration Requirements for Grants and Cooperative Agreements to State and Local Governments, Subpart C, Section .20, paragraph (a), (Standards for Financial Management Systems), and 44 CFR, Chapter 1, Part 13, Subpart C, Section 13.20, both require that a State must expend and account for grant funds sufficient to: (1) permit preparation of reports required, and (2) permit the tracing of funds to a level of expenditure adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes. 24 CFR, Part 570.490(a), requires the State to establish and maintain such records

as may be necessary to facilitate review and audit by the Department of Housing and Urban Development (HUD), and also audits in accordance with 24 CFR, Part 44.

Recommendation

Adequate documentation should be prepared and maintained for all requests for federal funds. Such documentation should permit the tracing of funds requested to a level of expenditure adequate to establish how the funds have been used. The personal notes and memory of an individual employee should not be a substitute for adequate documentation, and the records must provide for an accounting system which can be accessed and understood by other employees in the organization.

Item 4. Finding

Federal Cash Transaction Reports for Specific Grants Do Not Agree With the Department's Accounting Records

Seven out of ten Schedule of Federal Cash Transaction Reports as supported by the CDBG drawdown worksheets for CDBG grants submitted to HUD for the year ended June 30, 1993, did not agree with detailed accounting records maintained by the department's CALSTARS accounting system and CDBG drawdown worksheets. We were able to establish, however, that the total receipts of federal funds for the fiscal year are supported by the total expenditure of federal funds for the CDBG program.

Criteria

44 CFR, Chapter 1, Part 13, Subpart C, Section 13.41(c), requires that a Federal Cash Transactions Report (Form 272) be submitted. These reports are used by the federal agency to monitor cash advanced to grantees and to obtain disbursement or outlay information for each grant from grantees. These reports should reflect the grantee's performance, and be supported by accounting records. OMB Circular A-128 (8b.2) requires positive assurance that federal financial reports contain accurate, reliable financial data. The State Administrative Manual, Sections 20011 and 20014, requires all state agencies receiving federal funds to reconcile federal financial reports to the official accounting records and retain all supporting schedules and worksheets for a minimum of three years.

Recommendation

The CDBG drawdown worksheets maintained by the department's accounting office should be reconciled each month to both the SCO "R" accounts for receipts of federal funds, and the CALSTARS accounting records for the expenditure of federal funds.

Item 5.**The Department's Annual Cost Allocation Plan Has Not Been Updated and Approved for Two Years****Finding**

The department's annual cost allocation plan has not been developed and submitted to the Department of Finance and to HUD for approval for fiscal years 1991-92 and 1992-93. An indirect cost rate proposal for actual costs was presented to HUD (the federal cognizant agency) after the close of fiscal year 1992-93 which shows that the allocations used were within the guidelines for the total amount of the administrative costs of the grant and for the amount of matching expenses required. Actual costs were reasonably close to budgeted estimates.

Criteria

24 CFR, Parts 570.502 and 570.610, requires States to comply with OMB Circular A-87. OMB Circular A-87 requires local governments to establish a cost allocation plan to support the distribution of any joint costs related to the grant program, that all costs included in the plan will be supported by formal accounting records, and that this plan be retained at the local government level for audit by a designated federal agency except in those cases where that federal agency requests that the cost allocation plan be submitted to it for negotiation and approval.

Recommendation

The department should develop an updated cost allocation plan for fiscal year 1993-94.

Item 6.**Compliance With the Drug-Free Workplace Act Is Not Required of Grantees****Finding**

The department has not required that the subrecipients of CDBG grants comply with the Drug-Free Workplace Act of 1988.

Criteria

The Drug-Free Workplace Act of 1988 requires all subrecipients of federal grants to comply with the Drug-Free Workplace Act of 1988.

Recommendation

The requirements of the Drug-Free Workplace Act should be incorporated into the statement of assurances that subrecipients must sign prior to receiving CDBG grants, and consideration should be given to including this as a follow-up item during the grant monitoring process.

Department of Motor Vehicles

We reviewed the financial operations and related internal controls of the Department of Motor Vehicles (department).

Item 1. Inadequate Control Over Inventory Of Dishonored Checks

Finding

The department does not have sufficient control over its inventory of dishonored checks. According to the department's fiscal officer, as of June 30, 1993, the department had approximately 108,000 checks totaling \$23.6 million that banks had not honored. In our management letter for fiscal year 1991-92, we identified weaknesses in the department's process for recovering dishonored checks and stated that the weaknesses were caused by a lack of centralized control over the collection process. In response to our management letter, the department centralized the responsibility for processing dishonored checks for the Financial Responsibility Unit and the Drivers License Unit into a dishonored check unit. Furthermore, the department developed procedures for staff in these units to follow when processing dishonored checks.

In addition to implementing our recommendations, the department transferred the responsibility and authority for collection of delinquent vehicle registration fees to the Franchise Tax Board (FTB) as required by Section 10878 of the Revenue and Taxation Code. In September 1993, the department began sending all dishonored checks for vehicle registration that exceed \$300 to the FTB for collection. However, during our review we determined that the department is not periodically confirming with the FTB the dollar amount and number of dishonored checks that it transferred to the FTB for collection. As a result, the department cannot ensure that all of the dishonored checks for vehicle registration are accounted for.

Criteria

The California Government Code, Section 13403(a)(3), states that the elements of a satisfactory system of internal accounting and administrative controls should include, but are not limited to, a system of authorization and record keeping procedures that effectively control assets, liabilities, revenues, and expenditures.

Recommendation

The department should develop procedures to periodically confirm with the FTB the dollar amount and number of dishonored checks located at the FTB.

**Item 2.
Insufficient
Control Over
Access to EDP
Data Files**

Finding

The department's electronic data processing (EDP) programming personnel have unrestricted access to data files. For example, EDP personnel can access confidential and restricted data files even though such access is not necessary for these employees to fulfill their job duties.

In its response to the fiscal year 1991-92 management letter, the department stated that in January 1994, it would begin implementing a process to approve required access levels for programmers and restrict access to all other data files. However, as of April 1994, the department had not implemented any procedures to limit the programmer's access to data files. Furthermore, according to the information security officer, the department pushed back the implementation process indefinitely because of other priorities. Failure to restrict access to data files could result in possible disclosure or misuse of confidential and restricted information.

Criteria

The California Government Code, Section 11771, requires agencies to maintain strict controls over EDP systems to prevent unauthorized access to data files. In addition, the State Administrative Manual, Section 4841.3 states that automated files and data bases must be given appropriate protection from loss, inappropriate disclosure, and unauthorized modification.

Recommendation

The department should ensure that only authorized personnel have access to EDP systems and that such access is necessary for the performance of authorized duties.

Stephen P. Teale Data Center

We reviewed the financial operations and related internal controls of the Stephen P. Teale Data Center (data center).

Item 1. Failure To Record Software Costs as Intangible Assets

Finding

The data center records the cost of the software it purchases as an operating expense rather than an intangible asset. Intangible assets are assets that lack physical substance but give valuable rights to the owner. State regulations require state agencies to record software costs that exceed \$5,000 and that have a useful life of four years as intangible assets, and to systematically allocate the cost of the software to expenses over its useful life. Because the data center records its software purchases as expenses, it may overstate its operating expenses during years that it makes large software purchases. In addition, the cumulative effect of not recording intangible assets in the past was to understate assets (net of amortization) at June 30, 1993, by approximately \$4.8 million.

The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness during its audits for fiscal years 1988-89 through 1990-91. In its response in December 1993, the data center stated that it is in the process of developing and implementing policies to inventory and amortize intangible assets. As of April 1994, the data center has substantially completed its inventory of software, and is finalizing the process to amortize its intangible assets. The data center plans to complete this process so intangible assets and the related amortization can be included in its financial records at June 30, 1994.

Criteria

The State Administrative Manual, Section 8615.1, requires state agencies to record intangible assets that have an expected life of at least four years and cost at least \$5,000. Also, Section 8615 describes the costs of purchasing software as an intangible asset. Finally, the State Administrative Manual, Section 8621, requires proprietary funds such as the Stephen P. Teale Data Center Revolving Fund to record amortization. The State Administrative Manual, Section 8617, describes amortization as allocation of the cost of software, less its estimated residual value, to expense over the periods benefited.

Recommendation

The data center should record software costs that exceed \$5,000 as intangible assets and should allocate those costs to expense over the periods that it expects to use software to generate revenues.

Item 2. Possible Liability to the Federal Government

Finding

The data center has a possible liability to the federal government estimated to be as much as \$3.6 million for profits it has accumulated in its Stephen P. Teale Data Center Revolving Fund (revolving fund) between July 1, 1984, and June 30, 1993. The data center's revolving fund is an internal service fund that accounts for centralized electronic data processing services to state agencies. The data center has charged these agencies more than its costs for providing services. In turn, state agencies have passed these charges on to federal programs. The revolving fund accumulates profits when the data center's charges for services exceed its costs. Federal regulations prohibit the State from charging federal programs for more than its costs.

In addition, the data center may also owe the federal government for interest costs incurred by the data center in financing its equipment acquisitions. The unallowable interest charges totaled approximately \$1.5 million during fiscal years 1987-88 through 1992-93.

In 1984, the federal Department of Health and Human Services (DHHS) audited the State's rate-setting methods for internal service funds. As a result of the audit, the State was required to refund to the federal government approximately \$14.9 million of the profits accumulated in internal service funds. This amount represented the federal share of profits accumulated in five of the State's internal service funds from July 1, 1969, to June 30, 1984. The federal DHHS and the state Department of Finance agreed that 14.8 percent of the revolving fund's accumulated profits of approximately \$8 million at June 30, 1984, resulted from charges to federal programs and, thus, the revolving fund owed the federal government approximately \$1.2 million.

Currently, the federal DHHS is conducting an audit of the State's rate-setting methods for internal service funds for the period July 1, 1984, through June 30, 1991. As of April 30, 1994, the federal DHHS has not issued its final audit report.

Using procedures similar to those of the Department of Finance, and using the same ratio of 14.8 percent, we estimate that, under current federal regulations, the State may owe the federal government approximately \$3.6 million. However, an October 1988 proposed amendment to the federal Office of Management and Budget Circular A-87, would allow state agencies a reasonable working capital reserve of 60 days' worth of cash expenditures. This amendment, if approved, may reduce the liability to the federal government.

The data center also charged other state agencies for interest costs for equipment acquisitions. Federal regulations prohibit the State from charging interest costs to federal programs. We used the same ratio of 14.8 percent to estimate charges to federal programs for unallowable interest costs for equipment acquisitions during fiscal years 1987-88 through 1992-93. We concluded that the State may have an additional liability to the federal government, under current regulations, of approximately \$1.5 million for the federal share of interest costs for equipment acquisitions incurred by the data center during these fiscal years. For fiscal years 1984-85 through 1986-87, the data center did not separately disclose in its records interest costs for equipment acquisitions. Therefore, we did not calculate the State's potential liability to the federal government for the federal share of interest costs for those years.

During our audit, we found that the federal DHHS Division of Cost Allocation authorized a request from the State of Oregon to retain a 60-day working capital reserve, even though the revisions to OMB Circular A-87 have not been finalized. In January 1994, the State of California requested a similar authorization to retain a working capital reserve of 60 days' worth of cash expenditures. However, according to correspondence dated May 6, 1994, the federal DHHS Division of Cost Allocation will not respond to the State's request until the current federal audit is completed.

The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness during its audits for fiscal years 1988-89 through 1990-91. The state auditor and the auditor general recommended that the Department of Finance ensure state agencies comply with federal regulations. In his response of December 24, 1993, the director of the Department of Finance stated that, in some cases, state laws and regulations differ from those of the federal government and that the State is working with the federal government to minimize the differences. He stated that guidelines will be developed as soon as such differences are resolved. Also, in its

December 1993 response, the data center stated that effective July 1993, a system had been implemented which clearly identifies on each invoice whether any pass-through or rate-driven charges contain any costs which are not chargeable to federal reimbursement programs, and that the invoices state that the identified costs are not to be included in any requests for federal reimbursement.

Criteria

The federal Office of Management and Budget, Circular A-87, "Cost Principles for State and Local Governments," does not allow the State to charge federal programs for amounts that exceed costs. In addition, the California Government Code, Section 13070, provides the Department of Finance with general powers of supervision over all matters concerning the financial and business policies of the State.

Recommendation

The data center should comply with OMB Circular A-87 when establishing billing rates for charges to state agencies receiving federal support. Further, the Department of Finance should ensure that the data center complies with federal regulations. For example, compliance could be ensured by developing guidelines for the data center and state agencies receiving services from the data center. In addition, the Department of Finance should monitor the proposed amendment to OMB Circular A-87 to determine the effects the amendment may have on state charges to federal programs.

Item 3. Insufficient Documentation for Account Balances

Finding

The data center does not always maintain sufficient documentation for account balances. Specifically, the June 30, 1993, financial statements included installment contracts payable totaling \$8.7 million. However, the installment contract balance per the supporting detail totaled \$6.3 million. Data center staff were unable to provide any additional information that would support the balance included in the financial statements. As a result, the installment contract balance included in the June 30, 1993, financial statements was overstated by \$2.4 million.

Also, the financial statements included a Due From Other Funds balance of \$18.6 million. Again, the data center staff were unable to provide the accounting records which would support this amount, including the records identifying individual client credit balances included in the Due From Other Funds balance.

Criteria

The California Government Code, Section 13401, requires state agencies to maintain a system of internal accounting and administrative controls. The California Government Code, Section 13403, states that a satisfactory system of internal accounting and administrative controls includes a system of procedures adequate to provide effective accounting controls over assets, liabilities, revenues, and expenditures.

Recommendation

The department should comply with the requirements contained in the California Government Code to improve the accounting controls over its financial operations.

Item 4. Some Service Costs Not Fully Recovered

Finding

During previous audits of the data center, the Bureau of State Audits and the Office of the Auditor General reported that the data center did not always charge state agencies for services provided based on its published rate schedule. During fiscal year 1992-93, we found no further instances where this had occurred. Nevertheless, the data center has not made any attempts to collect the amounts undercharged in previous years or refund amounts overcharged to other agencies, although the data center significantly reduced its published rates twice during fiscal year 1993-94.

For fiscal year 1991-92, we reported that the data center had made an arrangement with the Governor's Office to charge a rate of \$250 per telecommunication line, as opposed to the published rate of \$905 per line. The data center's response was that the Governor's Office will be billed at the published rate beginning July 1994. As a result of the decreased rate, we estimate that the data center has lost revenues of approximately \$94,320 during fiscal years 1991-92 through 1993-94.

Also, for fiscal years 1987-88 through 1990-91, the Office of the Auditor General reported that the data center provided conversion processing and data base redevelopment services to the Department of Motor Vehicles, cumulatively worth approximately \$57 million. However, the data center only charged and collected approximately \$43 million so that the cumulative undercharge was approximately \$14 million.

Criteria

The State Administrative Manual, Section 8752, specifies that state policy requires agencies to recover full costs. All state agencies, regardless of funding sources, are required to follow this policy in all cases, except where statutes prohibit full cost recovery. Also, the State Administrative Manual, Section 4982.2, requires the State's data centers to charge their users for units of service based on their published service rate schedules.

Recommendation

The data center should recalculate charges for services provided to all its clients during the period July 1, 1987, through June 30, 1994, to ensure that all charges are equitable. Then, the data center should analyze the options available to collect underbillings from agencies not charged the full amount for services. Potential options may include negotiating a repayment plan with affected agencies, filing a claim with the State Board of Control, or requesting a special appropriation from the Legislature. Also, the data center should investigate the available methods to refund overcharges to agencies that were overbilled.

Department of Transportation

We reviewed the financial operations and related internal controls of the Department of Transportation (department) and the department's administration of the U.S. Department of Transportation grant, Federal Catalog Number 20.205.

Item 1. Federal Reimbursements for Contract Retentions Not Billed Promptly

Finding

The department did not promptly bill the Federal Highway Administration (FHWA) for the FHWA's share of certain costs for construction projects. Therefore, the department lost the use of up to \$11 million that it could have collected from the FHWA over the period from July 1989 to October 1992. As of March 31, 1994, up to \$6.5 million of this money has still not been collected. We performed further testing on \$6 million of the \$11 million and we estimate, on the \$6 million, the department lost approximately \$972,000 in interest earnings. For the remaining \$5 million, we did not perform additional testing; however, we estimate that the department's lost interest would not exceed \$808,000.

The department withholds a portion of progress payments owed to contractors for construction projects to ensure the contractors satisfactorily complete the projects. The department releases these withholdings, referred to as contract retentions, to the contractors when the contractors satisfactorily complete the projects or when the contractor has placed an amount equal to the contract retention in an escrow account. The department can bill the federal government for the amount of the contract retentions only after it releases the contract retentions to the contractors. However, we found that the department did not promptly bill the federal government for approximately \$11 million in contract retentions for 57 projects that we reviewed.

Although contract retentions are eligible to be billed to the federal government upon release, the department may not be able to bill the entire amount of the contract retention because the department cannot bill the federal government for costs which are in excess of the agreement for a federal aid project. Therefore, we applied some additional tests to \$6 million of the \$11 million billable amount and found that the \$6 million could have been billed to the FHWA because the related projects had not reached the agreement amount at the time the department released the retentions. We estimate that the department lost approximately \$972,000 in interest between the time the department could have received the \$6 million and March 31, 1994.

For the remaining \$5 million, we estimate that the department's lost interest earnings, depending on when the project costs reached the agreement amount, would not exceed \$808,000.

The Office of the Auditor General reported a similar weakness during its audit for fiscal year 1990-91. According to the chief of the department's construction payables branch, during October 1992, the department implemented a new method to set up these contracts in its system, and this new method was designed to prevent delayed billings. However, the method used to set up certain contracts in its construction contract payment system was incorrect, resulting in the delayed billings. The new method did not identify certain types of contract retentions that the department had released through the month of October 1992.

Criteria

The department's Accounting Manual, Chapter 12, states that when the department releases the contract retention for payment to the contractor, it should process that amount for billing to the FHWA. In addition, the State Administrative Manual, Section 0911.4, requires state agencies to bill the federal government promptly.

Recommendation

The department should collect this money as soon as possible and, in the future, the department should ensure that all costs eligible for reimbursement are promptly billed to the federal government.

Item 2. Final Claims Not Filed Promptly

Finding and Criteria

The department did not promptly submit some final claims to the Federal Highway Administration (FHWA) to close completed federal aid projects.

In August 1987, the department and the FHWA agreed that the department should submit final claims for its completed projects within 24 months of project completion. In February 1993, the department established an additional agreement with the FHWA to allow exemptions from the 24-month time requirement under certain circumstances. In this agreement, the department identified certain factors beyond its control which make it impossible to submit final claims within this time requirement. For 3 of the 21 federal aid projects completed between August 1987 and February 1993 that we reviewed, the department did not submit the final claim within 24 months of project completion. These three final claims were submitted 42, 49,

and 61 months after project completion and totaled approximately \$362,000. In addition, we found that the department submitted final claims that were 78 and 107 months after project completion for two of three federal aid projects we reviewed that were completed before or during August 1987. These two projects represent a group of long-outstanding projects for which the department continues to process final claims. Before the department and the FHWA's agreement in 1987, the department had a large backlog of projects awaiting final claims processing. Since that time, the department has reduced its backlog of projects to a level considered acceptable by the FHWA and continues to process final claims for long-outstanding projects. Although the department generally receives reimbursement for eligible project costs before it submits the final claim, the FHWA will not consider a project closed until it reviews and approves a final claim.

We identified the following additional factors which may contribute to the delay in submitting final claims.

- The department's district offices are required to complete expenditure reports for federal aid projects prior to processing the final claim. For 8 of the 28 federal aid projects that we tested at the San Francisco and Los Angeles district offices, the district office had not prepared preliminary or final expenditure reports within 120 days of either the after acceptance date of the project or the resident engineer's certification of the project completion and acceptance on the final progress payment voucher as required by the department's Accounting Manual.
- The department performs audits of certain types of federal aid projects prior to processing the final claim. In many cases, the department is taking longer than one year to complete these audits. Although there is no time requirement for completing an audit, the longer the audit remains outstanding, the less time the department's staff has to prepare the final claim.

The Code of Federal Regulations (CFR), Title 23, Section 140.107, required federal aid recipients to submit final claims promptly to the FHWA when the recipients complete projects. However, Title 23, Section 140.107, was removed from the April 1, 1993, edition of the CFR. According to an FHWA administrative manager, although Section 140.107 was removed from the 1993 edition of the CFR, the FHWA requirement to submit final claims promptly is still in effect,

based on the August 1987 agreement and United States Code, Title 23, Section 121(b) and (c), which addresses the requirement to submit a final voucher.

The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness during its audit for fiscal year 1990-91.

Recommendation

The department should submit final claims promptly to close completed federal aid projects.

Item 3. Receipt of Less Than Fair Market Value for Rented Airspace

Finding

The department is not receiving the fair market value for the rent of property located beneath a freeway. Such property is referred to as airspace. The department entered into three separate lease agreements in the 1970's with the Department of General Services (DGS) for the DGS to rent airspace beneath a freeway for state employee parking and vehicle storage. One of these leases expired in 1988 and the other two leases expired in 1989. Negotiations for renewing the leases have been on-going since 1987. The department determined the total fair market value for rental of the airspace to be \$27,305 per month. However, the DGS continues to use the property and in fiscal year 1992-93, paid a total of only \$8,359 per month, the total of the rates in effect at the end of the leases.

In March 1994, the department entered into three separate interim lease agreements with the DGS. The leases are for a six-month period for a total monthly rent of \$10,821. The department entered into these interim agreements in order to complete appraisals of the properties for the purpose of negotiating new long-term leases at fair market value.

Because the department is receiving less than the fair market value for the airspace, it cannot use the amount of the full fair market value for federal aid highway projects, as required by federal law. The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness during its audit for fiscal year 1990-91.

Criteria

The United States Code, Title 23, Section 156, requires states to charge, as a minimum, fair market value for the sale, use, lease, or lease renewals of airspace acquired as a result of a project funded in whole or

in part with federal assistance. Further, the section requires states to use the federal share of revenues received from such sales or leases for federal aid highway projects.

Recommendation

The department should continue to take steps to ensure that it receives the fair market value rate for the airspace it leases to the DGS.

Item 4. Noncompliance With State Requirements

Finding and Criteria

The department did not comply with administrative requirements of the State by not preparing accurate year-end financial reports in accordance with requirements of the State Administrative Manual. We found the following specific deficiencies for the fiscal year 1992-93 financial reports:

- The department did not correctly reconcile specific State Highway Account (SHA) budget items in the Final Reconciliation of the Controller's Accounts with Final Budget with the State Controller's Office balances.
- The department did not correctly report encumbrances of the SHA and the Transportation Planning and Development Account (TPDA) in the Report of Accruals to Controller's Accounts. As a result, the SHA encumbrances of approximately \$1.1 billion were overstated by approximately \$46 million and the TPDA's encumbrances of approximately \$242 million were overstated by \$1 million.
- The Claims Filed account per the Transportation Revolving Account (TRA) Pre-closing Trial Balance did not agree with the subsidiary records.
- The department used an incorrect account to reflect the accounts receivable balances for the SHA and the TRA. The SHA and the TRA Pre-closing Trial Balances showed debit balances of approximately \$3.3 million and \$4.2 million, respectively, in the Allowance for Uncollectable Accounts. The State Administrative Manual, Section 7620, provides specific account receivable accounts that agencies may use to account for receivables. The proprietary funds (enterprise and internal service funds) use the Allowance for Uncollectable Accounts classification to account for a reduction of receivables that will not be collected within the next fiscal year.

- The department did not record salaries and wages accrual reversals for fiscal year 1992-93. As a result, the Due to Payroll Revolving Fund balance for the TRA was overstated by approximately \$5 million.
- The department did not reconcile its fleet equipment expenditures with the changes in the fleet equipment inventory balances. The State Administrative Manual, Section 7969, requires agencies to reconcile equipment expenditures with the changes in the balance of the property account.
- The department did not correctly prepare the additions and deletions of fleet equipment in the Statement of Changes in General Fixed Assets (statement). The department's additions to and deletions from the statement of \$2.9 billion and \$2.8 billion respectively, did not accurately represent acquisitions or deletions of fleet equipment during fiscal year 1992-93. According to the department's Accounting Manual, Chapter 12, Section 5.7, in order to prepare the statement, control accounting creates a transaction each month using the current value of each unit in the fleet equipment as additions to the statement. A corresponding transaction is set up as a deletion which is intended to reverse the prior month's addition. However, the additions to and deletions from the statement actually represent the sum of the ending monthly balances of the fleet equipment for each of the 12 months, rather than the net additions and deletions for the year. The State Administrative Manual, Section 8660, requires agencies to report asset additions and asset deductions in the statement.

By not providing accurate information to the State Controller's Office, the department's financial reports will result in inaccurate financial statements for the State. The Department of Finance Management Memo 93-7, dated March 31, 1993, reminded agency officials of their responsibility for preparing accurate year-end financial reports. In addition, the State Administrative Manual, Sections 7950 through 7979, describes the requirements for preparing accurate financial reports.

Recommendation

The department should improve its compliance with the state requirements.

Education

California Community Colleges, Chancellor's Office

We reviewed the financial operations and related internal controls of the California Community Colleges, Chancellor's Office (Chancellor's Office), and the Chancellor's Office's administration of the U.S. Department of Education grant, Federal Catalog Number 84.048.

Item 1. Noncompliance With Certain State Requirements

Finding

We noted the following instances when the Chancellor's Office did not always comply with administrative requirements of the state government.

- The Chancellor's Office did not reconcile its physical inventory of property with its accounting records. Failure to reconcile the physical inventory with the accounting records can result in the failure to detect the loss or theft of state property. The Office of the Auditor General reported a similar weakness during its audit of fiscal year 1990-91. The State Administrative Manual, Section 8652, requires that agencies reconcile the physical property counts with the accounting records at least once every three years.
- The Chancellor's Office has not taken steps to clear long-outstanding travel and expense advances made from the revolving fund. During our review, we noted that several items totaling approximately \$14,000 had been outstanding for more than one year. The Office of the Auditor General reported a similar weakness during its audits for fiscal years 1988-89 through 1990-91. The State Administrative Manual, Section 8116, requires agencies to reimburse and, therefore, clear advances from the records when employees submit their travel expense claims.

Although individually these deviations may appear to be insignificant, they do represent noncompliance with state regulations, which are designed to protect the public's resources from abuse.

Recommendation

The department should improve its compliance with state requirements.

California Postsecondary Education Commission

We reviewed the California Postsecondary Education Commission's (commission) administration of the U.S. Department of Education grant, Federal Catalog Number 84.164.

Item 1. Inadequate Procedures for Monitoring Cash Advances to Grantees

Finding

The commission does not always ensure that cash advanced to grantees participating in the Eisenhower Mathematics and Science Education—State Grants program (program) is limited to the grantees' immediate cash requirements. Specifically, the commission's procedures allow it to advance grantees two payments totaling 90 percent of the award over two six-month periods. In addition, the commission pays the final 10 percent after receiving the annual program and fiscal reports. Further, if need is shown, the grantee may request more than 90 percent prior to submitting the final reports. However, the commission pays the grantees three installments of 60 percent, 30 percent, and 10 percent, irrespective of the grantees' cash on hand. We reviewed payments to seven grantees and found that the commission paid two grantees more than the grantees needed or requested.

One grantee reported a cash balance of approximately \$66,400 and requested no funds. However, the commission paid the grantee an additional \$66,400. As a result, the commission paid the grantee 98 percent of the year's grant although there was no evidence that the grantee showed a need for additional funds.

The commission advanced another grantee approximately \$136,700, the first 60 percent of the grant. In its second request for funds, the grantee reported a cash balance of \$121,800. In accordance with the commission's cash advance procedures, the grantee requested \$68,300, the next 30 percent of the grant. Although the grantee reported a large cash balance, the commission paid \$68,300 to the grantee, the full amount requested. In the next request, the grantee requested the final 10 percent of grant funds even though the grantee reported cash on hand of approximately \$172,600. The commission paid the final 10 percent even though the grantee had not yet submitted its final program and fiscal reports.

Criteria

The Code of Federal Regulations, Title 34, Section 80.20(b)(7), requires procedures for minimizing the time elapsing between the transfer of funds from the U.S. Treasury and disbursement by the

commission be followed whenever advance payment procedures are used. Further, Section 80.20(b)(7) requires the commission to monitor cash drawdowns by the grantees to ensure that they conform substantially to the same standards of timing and amount as apply to advances to the commission.

Recommendation

The commission should limit cash advances to the immediate needs of the grantees.

Item 2. Lack of Documentation To Support Personnel Costs

Finding

The commission lacked documentation to support the personnel costs charged to the program. For all five employees that we tested, the commission did not maintain records to support the amounts charged to the program. The commission estimated that the employees spend from 5 percent to 90 percent of their time on the program. Unless the commission documents the time employees spend on the program, the commission may not charge the correct personnel costs.

The United States Department of Education reported a similar finding for one employee in its report dated June 17, 1992. In its response, the commission stated that under state personnel policies, no specific time records are maintained for any persons in a work group not related to a 40-hour work week.

Criteria

The Office of Management and Budget (OMB), Circular No. A-87, Attachment B, Section B(10)(b), requires amounts charged to grant programs for personal services, regardless of whether treated as direct or indirect costs, be based on payrolls documented and provided in accordance with generally accepted practices of the State. Further, Section B(10)(b) states that payrolls must be supported by time and attendance or equivalent records for individual employees. Also, Section B(10)(b) requires salaries and wages of employees chargeable to more than one grant program or other cost objective be supported by appropriate time distribution records.

Recommendation

The commission should document personnel costs charged to the program by time and attendance or equivalent records for individual employees.

Item 3. Finding
Weaknesses in Separating Accounting Duties
The commission does not have adequate separation of duties in its accounting section. Specifically, the employee who deposits cash receipts also prepares checks and invoices. Further, the commission has weaknesses over the purchasing function. Two employees jointly handle both purchasing and receiving. Finally, one employee approves claim schedules for payment and records expenditures.

Without the proper separation of duties, an employee could conceal errors or irregularities, and management may be unable to determine who is responsible for the errors or irregularities.

Criteria
The State Administrative Manual, Section 8080, prescribes the appropriate level of separation of duties for agencies with manual accounting systems. This section specifies that an employee who receives or deposits cash receipts is not to prepare checks or invoices. In addition, Section 8080 states that, when necessary, employees of units other than the accounting unit should be used to provide separation of duties. Finally, the California Government Code, Section 13401, requires state agencies to maintain a system of internal accounting and administrative controls. Good internal controls require the separation of the following functions: purchasing and receiving merchandise, approving invoices for payment, disbursing funds, and recording expenditures.

Recommendation
The commission should separate its accounting duties to comply with the requirements of the California Government Code and the State Administrative Manual. Further, the commission should use personnel from outside the accounting unit, if necessary, to achieve proper segregation of duties.

Item 4. Finding
Delay in Disbursing Federal Grant Monies
The commission's cash management system does not minimize the amount of time between receiving federal funds and disbursing them to grantees. We tested 10 claims to determine the amount of time between receipt and disbursement. We found that for 8 claims, the State was from one to six days late in disbursing the funds, for an average delay of 2.8 days.

Criteria

The Code of Federal Regulations, Title 31, Section 205.4(a), requires that the timing and amount of cash advances be as close as administratively feasible to the actual disbursements by the recipient organization. We consider a delay of no more than five working days as administratively feasible.

Recommendation

The commission should implement procedures that will minimize the time elapsed between receipt of federal funds and disbursement to grantees.

Item 5. Noncompliance With Other Federal and Department Requirements

Finding and Criteria

We noted the following instance where the commission did not always comply with administrative requirements of the federal government and the commission:

- We reviewed seven grantee files. For four of the seven grantee files, the commission could not provide two annual fiscal reports, one mid-year fiscal report, and two program update reports. Unless the commission obtains required reports from the grantees, the commission cannot ensure that grantees comply with federal requirements and grant conditions. The Code of Federal Regulations, Title 34, Section 80.40(a), requires the State to monitor activities to ensure that grantees comply with applicable federal requirements and achieve performance goals. Also, as part of its monitoring and grant conditions, the commission requires grantees to submit mid-year program and fiscal reports and an annual report.

Recommendation

The commission should improve its compliance with federal and commission requirements.

California Student Aid Commission

We reviewed the California Student Aid Commission's (commission) administration of the U.S. Department of Education grant, Federal Catalog Number 84.032.

Item 1. A Student Loan Exceeded the Allowable Limit

Finding

During fiscal year 1992-93, the commission guaranteed and disbursed at least one individual student loan that exceeded the allowable federal loan limit. We selected a subset of more than 34,000 student loans that had the potential of exceeding federal loan limits from the commission's database of students participating in the Stafford Loan Program, Supplemental Loans to Students Program, and the Parent Loan Program. From the subset, we randomly selected 60 student loans for review. Of these 60 loans, the commission guaranteed and disbursed a loan that exceeded the limit for one Stafford loan borrower. The loan guarantee and disbursement exceeded the established limit by a total of \$875. The borrower was enrolled in a course of less than a full year and the prorated federal loan limit was exceeded. Specifically, according to school officials, the student was enrolled in a course of only 14 weeks. According to allowable federal loan limits for Stafford loans, the student was eligible for a Stafford loan of only \$875. However, the commission guaranteed and disbursed a loan for \$1,750. Noncompliance with federal loan limits could result in a loss of state funds if the borrower defaults. If the borrower defaults, the federal government may not purchase from the commission the portion of defaulted loans above the limit.

The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness during its audits for fiscal years 1989-90 and 1990-91.

Criteria

The United States Code, Title 20, Sections 1078, 1078-1, and 1078-2, provides for specific loan limits for guaranteeing Stafford, Supplemental Loans to Students, and Parent Loan Program loans. These limits are based on the student's grade level, the length of the course in which the student is enrolled, and the total outstanding principal for each loan program.

Item 2.
**Failure To Ensure
That Defaulted
Student Loans
Met Federal
Requirements for
Reimbursement**

Recommendation

The commission should guarantee and disburse only loans that are within the applicable federal limits.

Finding

The commission did not always ensure that it met the federal 90-day guidelines for paying lenders for defaulted loans. Of the 39 loans that we reviewed, we found that the commission did not pay the lenders of 13 loans (33 percent) within the required 90 days from the date the lenders submitted their default claims to the commission. The commission paid the 13 claims an average of 16 days late. Failure to ensure that loans meet federal requirements could jeopardize federal reimbursement. The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness during its audits for fiscal years 1987-88 through 1990-91.

Criteria

The Code of Federal Regulations, Title 34, Section 682.406(a), lists the conditions that must be met to qualify a defaulted student loan for federal reimbursement. These conditions include the requirement that the commission pay the lender within 90 days of the date the lender filed the claim.

Recommendation

The commission should ensure that all defaulted student loans it submits for reimbursement to the federal government meet the federal requirement for payment within 90 days.

Item 3.
**Ineffective System
for Preventing
Collection
Agencies From
Providing
Conflicting
Services on the
Same Loan**

Finding

The commission did not have an effective system to prevent collection agencies from collecting on the same student loans for which the agencies provided supplemental preclaims assistance. Supplemental preclaims assistance consists of specified procedures used to persuade severely delinquent borrowers to repay rather than default on their loans. For three of the ten loans that we reviewed, the commission assigned the same collection agency that provided supplemental preclaims assistance to collect on the loan. If the same agency that performed the preclaims assistance also collects the loan, the federal government could refuse to reimburse the commission for the cost of

supplemental preclaims assistance for the loan. The Office of the Auditor General reported a similar weakness during its audits for fiscal years 1988-89, 1989-90, and 1990-91.

Criteria

The Higher Education Act, Section 428(c)(6)(C)(iii), requires that supplemental preclaims assistance be done by an organization or entity that does not have a contract with the commission to perform collection activities for the same loans in the event of default.

Recommendation

The commission should ensure that loans are not assigned for collection activities to the same collection agency that provided supplemental preclaims assistance.

Item 4. National Credit Bureaus Do Not Always Accurately Record Information About Defaulted Loans

Finding

The commission did not ensure that credit bureaus accurately recorded information about defaulted student loans. The commission reports information about defaulted student loans to three national credit bureaus with which it contracts. Although its records indicated that the commission had sent the information to the credit bureaus, the records did not indicate the specific credit bureaus to which the commission reported the information. Therefore, we reviewed the records of the three credit bureaus for 12 loans to verify that they had received the information. For 10 of the 12 loans, either one or two of the credit bureaus did not have any record of the defaulted loans being reported. Without documentation that the credit bureaus received the information or that the commission verified that credit bureaus accurately recorded the information the commission reported, we cannot conclude that the commission properly reported defaulted loans.

Further, the commission did not ensure that the correct total amount and the outstanding balance for one of the 12 loans was reported correctly by one credit bureau. Specifically, the credit bureau reported the balance of the loan more than \$200 less than the actual claim paid.

Finally, the commission did not ensure that one credit bureau correctly reported the information concerning loan collection. Specifically, we found that for all 12 loans that we reviewed, one credit bureau assigned an incorrect status code to each loan. Credit bureaus use status codes to indicate, for example, whether a loan has been charged to bad debt or is a collection account. The credit bureau assigned status codes to these 12 loans for which there was no meaning.

If a credit bureau does not properly report information regarding defaulted loans, a lender or other guarantee agency could use incorrect information when making or insuring loans.

The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness during its audits for fiscal years 1988-89 through 1990-91. In its response dated June 4, 1992, to the audit for fiscal year 1990-91, the commission stated that it was researching similar concerns with its credit bureaus.

Criteria

The Code of Federal Regulations, Title 34, Section 682.410(b)(3), requires the commission to report to all national credit bureaus the default date, information concerning loan collection, and the date the loan is fully repaid or discharged. In addition, the Higher Education Act, Section 430(A)(a), requires the commission to report to all national credit bureaus the total amount of loans made to any borrower and the remaining balance of the loans.

Recommendation

Based on the results of its research, the commission should determine whether it should continue to report loans to credit bureaus that do not accurately record information.

Item 5. Federal Quarterly and Monthly Reports Are Not Reconciled With Each Other or With Accounting Records

Finding

The commission did not ensure that information on its federal reports agreed with either other federal reports or with its accounting records. For example, the commission's federal reports for April through June 1993 contained information that did not agree with the commission's accounting records. Specifically, the commission reported in the Guarantee Agency Quarterly Report (1130 Quarterly Report) paid lender claims totaling \$123,642,000. The commission's accounting records, however, showed paid lender claims totaling \$123,855,432, a difference of \$213,392. Furthermore, in the 1130 Quarterly Report, the commission reported collections totaling \$45,917,229 while its accounting records showed collections totaling \$45,644,265, a difference of \$272,964. Because the commission did not provide us with a reconciliation from the 1130 Quarterly Report to the accounting records, we could not determine whether the quarterly report, the accounting records, or both, were inaccurate. The Bureau of State Audits reported a similar weakness in the audit for fiscal year

1991-92, and the Office of the Auditor General reported a similar weakness during its audits for fiscal years 1986-87 through 1990-91.

In addition, in its Guarantee Agency Monthly Reports (1189 Monthly Report) for April through June 1993, the commission reported a total of \$123,940,439 in paid lender claims and a total of \$44,388,724 in collections received. The amount the commission reported for paid lender claims in its 1189 Monthly Reports was \$298,399 more than the amount it reported in its 1130 Quarterly Report. Also, the amount the commission reported for collections received in its 1189 Monthly Reports was \$1,528,505 less than the amount it reported in its 1130 Quarterly Report. Because the commission did not provide us with a reconciliation from the 1130 Quarterly Report to the 1189 Monthly Reports, we could not determine whether the quarterly report, the monthly reports, or both, were inaccurate.

Finally, although it was able to reconcile the portion of the 1189 Monthly Report for April concerning claims paid to its accounting records, the commission did not reconcile the portion concerning collections received to its accounting records. Specifically, in its 1189 Monthly Reports for April, May, and June of 1993, the commission reported collections totaling \$44,388,724, yet its accounting records showed collections for this same period totaling \$45,644,265, a difference of \$1,255,541. Because the commission did not provide us with a reconciliation from the portion of the 1189 Monthly Report concerning collections received to its accounting records, we could not determine whether the monthly reports, the accounting records, or both, were inaccurate.

Criteria

The Code of Federal Regulations, Title 34, Section 682.414(b), requires the commission to accurately complete and submit reports that concern the status of the commission's loan guarantee program. Further, the State Administrative Manual, Section 20014, requires agencies receiving federal funds to reconcile federal financial reports with the official accounting records.

Recommendation

The commission should reconcile its quarterly reports and monthly reports to one another and to its accounting records.

Item 6. Noncompliance With Additional Federal Requirements

Findings and Criteria

We noted the following instances when the commission did not always comply with administrative requirements of the federal government:

- The commission did not report at least \$16.4 million (more than 35 percent) of the amount of the collections due the federal government for the 1992-93 fiscal year within the required time period. The Code of Federal Regulations, Title 34, Section 682.404(e)(4), requires the commission to submit the federal share of borrower payments within 60 days of receipt. The time limit was reduced to 45 days, effective February 19, 1993. The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness during its audit for fiscal year 1990-91.
- The commission did not ensure that all Guarantee Agency Federal Quarterly Reports were submitted within the required 60-day time limit. The reports for the March and June 1993 quarters were 183 and 92 days late, respectively. We observed that the September 1993 quarterly and annual report, although outside the scope of the audit, was submitted within the required 60-day limit. Instructions from the U.S. Department of Education require that Guarantee Agency Federal Quarterly Reports be submitted within 60 days after the end of each quarter of the year.

Recommendation:

The commission should improve its compliance with federal regulations.

California Department of Education

We reviewed the financial operations and related internal controls of the California Department of Education (department) and the department's administration of the U.S. Department of Agriculture grants, Federal Catalog Numbers 10.550, 10.553, 10.555, and 10.558; the U.S. Department of Labor grant, Federal Catalog Number 17.250; the U.S. Department of Education grants, Federal Catalog Numbers 84.010, 84.011, 84.027, 84.048, 84.151, 84.164, 84.173, and 84.186; and the U.S. Department of Health and Human Services grant, Federal Catalog Number 93.575 (formerly 93.037).

Item 1. Inadequate Procedures To Ensure That Cash Advances are Limited to Immediate Needs and That Billings for Overpayments are Done Promptly for the Payments to States for Child Care Assistance Program

Finding

The department's procedures do not ensure that cash advanced to local assistance contractors participating in the Payments to States for Child Care Assistance program is limited to the contractors' immediate cash requirements. Instead, the department makes monthly payments to contractors but does not do a monthly analysis of contractors' actual needs. Furthermore, the department does not promptly bill contractors that it overpaid.

The department's procedures allow it to advance contractors up to one-twelfth of their annual "Maximum Reimbursable Amount" (MRA) each month. The MRA is the maximum amount that the department will pay the contractor for the period of the contract. The contractors submit monthly attendance and fiscal reports that the department should use to calculate the amount of the advance that the contractor has earned each month based on the number of child care services the contractor provided. Depending on the results of these calculations, the department could provide additional monthly advances to the contractor or reduce future monthly advances by any amount down to zero if it paid the contractor more than it earned in prior months. However, the department does not perform the calculation each month to determine if contractors earned the full amount of the advance. Rather, the department makes monthly payments of one-twelfth of the contractor's MRA each month beginning in July, but it does not perform any calculations of the amounts earned until six months later when it receives the December report from contractors.

We reviewed year-end attendance and fiscal reports for 22 contractors and found that the department paid 8 contractors more than the contractors supported in their attendance and fiscal reports. For

example, one contractor was paid \$63,666 more than it earned. This occurred because the contractor did not provide the amount of services that it originally planned to provide.

Of the eight contractors that the department overpaid, the department has not taken any action to recover the overpayments from five contractors and it billed the three other contractors from five to nine months after the close of the fiscal year.

Criteria

The Code of Federal Regulations, Title 34, Section 80.20(b)(7), requires that the timing and amount of cash advances be as close as possible to the actual disbursement by the recipient organization. Once the department recognizes that the contractor has not used its entire cash advance, the State Administrative Manual, Section 8776.3, requires agencies to prepare and send out an invoice or other type of claim document as soon as possible after recognition of a claim in order to have the unused funds returned.

Recommendation

The department should change its procedures so that it calculates the amount of reimbursement earned by the contractors starting with the first month's attendance and fiscal reports. In addition, the department should take prompt action to reduce subsequent monthly payments for those contractors the department has paid more than the contractor has earned. Furthermore, the department should promptly bill those contractors whose end-of-year calculation shows that they have been paid more than they earned.

Item 2. Inadequate Procedures for Determining the Amount of Federal, State, and Local Funds Expended During the Base Year and Fiscal Year 1992-93 for the Payments to States for Child Care Assistance Program

Finding

The department's procedures for determining the amount of federal, state, and local funds expended for child care and related services for the base year and fiscal year 1992-93 for the Payments to States for Child Care Assistance program do not ensure that actual expenditures are accurately determined and reported. The base year is defined as the year prior to the first year that the grant was provided to the State. For the Payments to States for Child Care Assistance program in California, the base year is fiscal year 1990-91. The base year expenditure levels are used as a reference to determine if other federal, state, or local expenditures for child care related services are reduced in subsequent years. A reduction in these expenditures could indicate that Child Care Payments to States funds are being used inappropriately to supplant rather than supplement other federal, state, or local funds.

The department stated in a revision of its fiscal year 1992-93 grant application that its reported expenditures for the base year are budgeted expenditures and that the fiscal year 1992-93 figures are actual expenditures. However, the department actually used a mixture of budgeted, actual, and estimated expenditures to calculate the expenditures reported for both of these years, instead of using actual expenditures as required.

We determined the department's federal and state expenditures that the department should have reported for the base year and fiscal year 1992-93 based on actual expenditure data available at the department. However, we did not determine the actual expenditures of the Department of Social Services, which also operates child care related programs and reports its data to the department to be included in the department's reports. Furthermore, we did not calculate expenditures of local funds because the department does not have local expenditure data. Our calculations revealed that actual expenditures were lower than was reported for federal and state expenditures for both the base year and fiscal year 1992-93. The expenditures reported by the department and our calculation of expenditures are as follows:

**Reported by the
California Department of Education
(In Millions)**

	Base Year	Fiscal Year 1992-93
State	\$ 362.8	\$ 429.0
Federal	214.5	341.2

**Calculated by the
Bureau of State Audits
(In Millions)**

	Base Year	Fiscal Year 1992-93
State	\$351.4	\$ 403.1
Federal	214.1	278.5

There is no evidence that the department used Child Care Payments to States funds to supplant other federal or state funds based on the State's reported expenditures or based on our calculation of expenditures. However, if the department does not determine the actual amount of expenditures for the base year and subsequent years, it will be unable to determine if supplanting of other federal, state, or local funds with federal funds occurred.

Criteria

The Code of Federal Regulations, Section 98.53(a), requires states to provide assurances that funds will not be used to supplant the amount of federal, state, and local funds otherwise expended for child care services and related programs. Section 98.53(b) requires states to determine and report the amount of funds expended for a base period and for subsequent periods and to ensure that expenditures in subsequent periods are maintained at least at the levels for the base period.

**Item 3.
Delay in
Disbursing
Federal Grant
Monies**

Recommendation

The department should use actual expenditure data from its own accounting system and obtain actual expenditure data from the accounting systems of other state agencies to calculate the amount of federal and state expenditures that it reports to the federal government.

Finding

The department's cash management system does not minimize the amount of time between receiving federal funds and disbursing them to subrecipients. We tested 269 claims to determine the amount of time between receipt and reimbursement. We found that, for 64 claims, the State was from one to 13 days late in disbursing the funds. We consider a disbursement late if it is delayed more than five days after the receipt of federal funds. The department was late an average of 2.46 days, which is an improvement from the 3.15 days that we reported during our audit for fiscal year 1991-92.

The Office of the Auditor General reported similar weaknesses during its audit for fiscal years 1987-88 through 1990-91. In its response to that finding, the department stated that it anticipates no further improvement in the timeliness of disbursing federal funds until the State Controller's Office changes its policy of requiring federal cash to be on deposit in the State Treasury prior to the department's submission of claims to the State Controller's Office.

Criteria

The Code of Federal Regulations, Title 31, Section 205.4(a), requires that the timing and amount of cash advances be as close as administratively feasible to the actual disbursement by the recipient organization.

Recommendation

The department should improve its compliance with federal regulations by minimizing the delay between the receipt of federal funds and the actual disbursement.

Item 4. Weakness in Contracting Procedures Within the Healthy Kids, Healthy California Office

Finding

The department has not ensured that federal funds are used only for allowable services. The department receives funds from the Drug-Free Schools and Communities—State Grants, a grant whose use is restricted to education on illegal drug and alcohol use prevention. We reviewed all nine of the contracts that the department entered into in fiscal year 1992-93 that used Drug-Free Schools and Communities—State Grants funds. One of the nine contracts requires the contractor to perform four tasks. Although three of the four tasks relate clearly to services allowed under the Drug-Free Schools and Communities—State Grants, one of the tasks is only partially allowable. That task calls for a review of the outcome of training conferences and a Course Resource Binder. The Course Resource Binder is a resource manual for teacher preservice education in health and addresses a wide range of comprehensive health education issues including one chapter on alcohol, tobacco, and other drugs. Although the department used federal drug-free schools funds and state funds for this contract, neither the contract nor other department records provide any means to determine how these funds are to be allotted for the work required under the contract. Since at least a portion of the contract was for comprehensive health education issues, the department should have identified the portion that was an allowable use of the Drug-Free Schools and Communities—State Grants funds and identified the portion that the state funds would support.

We reported a similar contracting weakness during our audit for fiscal year 1991-92. In its response to that finding, the department stated that it would require separate budgets for each funding source in all new contracts.

Criteria

The United States Code, Section 3194(b), provides funds for training and technical assistance programs concerning drug abuse prevention, the development and distribution of material teaching that drug use is harmful, demonstration projects in drug abuse education and prevention, special financial assistance to enhance resources available for drug abuse prevention in certain areas, and for administrative costs of the State. Also, the U.S. Department of Health and Human Services has distributed nonregulatory guidance for the Drug-Free Schools and Communities—State Grants which states that agencies may choose to include drug and alcohol abuse education and prevention as part of a comprehensive health education program; however, the expenditure of Drug-Free Schools and Communities—State Grants funds must be limited to that part of the program dealing with drug and alcohol abuse

education and prevention. Further, the Code of Federal Regulations, Title 34, Section 80.20(a)(2), requires that the State and its subgrantees keep records to permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of grant restrictions.

Recommendation

When the department enters into contracts that use state funds along with Drug-Free Schools and Communities—State Grants funds, it should clearly identify in the contract the portion that it will pay with federal funds and the portion that it will pay with state funds.

Item 5. The Department Has Not Fully Implemented Its Proposed Actions To Resolve Weaknesses in Its Monitoring of Local Educational Agencies That Were Identified by the U.S. Department of Education in 1992

Finding

In June 1992, the U.S. Department of Education (USDOE) reported that the department did not systematically monitor the Local Educational Agencies (LEA) participating in the Eisenhower Mathematics and Science Education—State Grants program. The USDOE recommended that the department develop a program to systematically monitor the LEAs for compliance and program quality.

We reported this weakness during our audit for fiscal year 1991-92. In its response to our report dated November 10, 1992, the department stated that it was developing a plan to systematically monitor LEAs. The plan will include a pattern and timetable for site visits and telephone calls. Additionally, the plan will include a sampling of LEAs to be evaluated each year. However, we found that the plan that the department developed does not include a timetable for site visits or telephone calls, nor does it include a sampling of LEAs to be evaluated each year. Furthermore, the plan does not indicate that the department will monitor LEAs for compliance with federal requirements such as ensuring that children and teachers from private, nonprofit schools have equitable participation in the Eisenhower Mathematics and Science Education—State Grants program or that LEAs use Eisenhower program funds to supplement and not supplant other federal, state, or local funds.

When the department does not sufficiently monitor LEAs, it cannot ensure that they are complying with federal requirements.

Criteria

The Code of Federal Regulations, Title 34, Section 80.40(a), requires grantees to monitor activities to ensure that LEAs comply with applicable federal requirements and that they achieve performance

goals. The Code of Federal Regulations, Title 34, Subpart F, Sections 208.51(a) and (b), requires that LEAs shall make provisions for ensuring the equitable participation for children and teachers from private, nonprofit schools in the benefits of the Eisenhower Mathematics and Science Education—State Grants program. The Code of Federal Regulations, Title 34, Section 208.41(b), requires that subgrantees do not use federal funds to supplant funds from nonfederal sources.

Recommendation

The department should fully develop and implement its plan to monitor LEAs to ensure that LEAs comply with applicable federal regulations and achieve performance goals.

Item 6.

Insufficient Control Over Expenditure Reports From Local Educational Agencies Participating in the Eisenhower Mathematics and Science Education—State Grants Program

Finding

The department does not ensure that all LEAs submit expenditure reports by the due date and does not ensure that the expenditure reports are accurate. Also, the department does not promptly bill school districts for unused funds for the Eisenhower Mathematics and Science Education—State Grants program. We selected for review 30 LEAs that should have submitted expenditure reports during fiscal year 1992-93 and found the following:

- As of December 15, 1993, all 30 of the LEAs that we tested had submitted the required expenditure reports; however, 9 LEAs submitted the reports late. The period of the late reports ranged from 13 to 100 days. If the expenditure reports are not submitted promptly, the department cannot promptly determine whether the LEAs spent all funds paid or should return unused funds.
- In addition to late submissions, we found that some of the expenditure reports were inaccurate. The department relies on the expenditure reports to identify unused funds that should be returned to the department and, in turn, to the federal government. None of the LEAs' expenditure reports indicated that they had any unused funds from the fiscal year 1992-93 entitlement that they must return. However, the expenditure reports from three LEAs should have indicated that they had unused funds from prior years' entitlements that should have been returned. Our calculations revealed that the amount of the funds that should have been returned ranged from \$413 to \$2,785. As of December 1993, the department had not detected these collectable amounts nor billed

the LEAs for the unused funds. As a result, the LEAs are holding excess federal funds that should be returned to the federal government.

We reported a similar weakness during our audit for fiscal year 1991-92. In its response to this finding, the department stated that the addition of two clerical support positions will speed the processing time and ensure prompt follow-up on unreceived expenditure reports and billing of LEAs for unused Eisenhower program funds.

Criteria

The Code of Federal Regulations, Title 34, Section 76.722, states that a state may require an LEA to furnish reports that the state needs to carry out its responsibilities under the program. The department required that the LEAs submit an expenditure report for fiscal year 1992-93 with a due date of August 12, 1993. Additionally, the Code of Federal Regulations, Title 31, Section 205.4(a), requires that the timing and amount of cash advances be as close as administratively feasible to the actual disbursement by the recipient organization. Once the department recognizes that the recipient organization has not used its entire cash advance, the State Administrative Manual, Section 8776.3, requires agencies to prepare and send out an invoice or other type of claim document as soon as possible after recognition of a claim in order to have the unused funds returned.

Recommendation

The department should ensure that all LEAs submit expenditure reports promptly. Additionally, the department should ensure that expenditure reports are accurate. Furthermore, the department should promptly bill the LEAs for any unused funds.

**Item 7.
Inadequate
Procedures for
Reviewing
Community Based
Organizations,
Audit Reports for
the Job Training
Partnership Act
State Education
Coordination and
Grants 8 Percent**

Finding

The department's procedures for reviewing audit reports submitted by Community Based Organizations (CBO) do not ensure that reports are reviewed in a timely manner for the Job Training Partnership Act State Education Coordination and Grants 8 Percent. Sixteen CBOs should have sent audit reports for fiscal year 1991-92 to the department by November 15, 1992. However, as of May 1994, the department has received only 11 audit reports. Within 30 days from the date that the department receives the audit report, the department's procedures require that it send an "Initial Determination" which identifies each specific issue to those CBOs whose audit reports identified deficiencies. However, as of May 1994, even though the audit reports identified compliance or internal control deficiencies, the department has not sent any "Initial Determinations." If the department does not take prompt action to require CBOs to correct deficiencies noted in the audit reports, it cannot ensure that the CBOs will correct the deficiencies, nor can it recover any excess funds or take any other required financial actions.

Criteria

The Code of Federal Regulations, Title 34, Section 80.40(a), requires grantees to monitor activities to ensure that LEAs comply with applicable federal regulations and that they achieve performance goals. Additionally, the Office of Management and Budget (OMB) Circular A-133 states that state governments that allocate \$25,000 or more of federal financial assistance to nonprofit institutions must ensure that the nonprofit institutions obtain an independent audit that determines whether federal financial assistance was spent in accordance with applicable laws and regulations. Furthermore, the department's contractual agreement with LEAs requires that LEAs submit the audit reports to the department by November 15. This same contractual agreement requires the department to send Initial Determinations within 30 days of receipt of the audit report.

Recommendation

The department should ensure that CBOs submit audit reports when required and improve procedures to ensure prompt internal review of the audit reports. Furthermore, the department should send Initial Determinations within 30 days to those CBOs whose audit reports identified deficiencies.

Item 8. Weaknesses in the Department's Monitoring of Charitable Institutions, Nonprofit Summer Camps, and Food Processors for the Food Distribution Program

Finding

The department does not always schedule required program reviews or ensure the timely completion of program reviews of charitable institutions, nonprofit summer camps, and food processors for the Food Distribution program.

For our audit testing, we selected 10 of the 34 food processor program reviews that the department conducted in fiscal year 1992-93. Additionally, we reviewed a department listing that identified all 808 of the charitable institutions and nonprofit summer camps that the department was required to review within the last four years to determine if the department conducted the required reviews.

In our testing of food processor program reviews, we found that the department conducted one of the reviews two years after the date required by federal regulations. In our review of the department's listing of institutions and summer camps that required reviews within the last four years, we found that two charitable institutions were two years overdue the required program review. We also found that the department has never reviewed one of the charitable institutions on the listing. The department does not know when this charitable institution began its participation in the program and, therefore, does not know when the program review is required. Finally, our review of the listing revealed that the department has never conducted a program review of one nonprofit summer camp that has been participating in the program since 1974.

Criteria

The Code of Federal Regulations, Title 7, Sections 250.19(b)(i) and (ii), requires that the department perform on-site reviews of charitable institutions and nonprofit summer camps once every four years with no fewer than 25 percent of the reviews completed per year. Additionally, the department must review food processors at least once every two years, with no fewer than 50 percent being reviewed each year.

Recommendation

The department should ensure that it conducts reviews of all institutions when required and retain documentation for the reviews that it conducts.

**Item 9.
Weaknesses in the
Department's
Procedures for
Ensuring the Food
Distribution
Institutions Take
Prompt Corrective
Action for
Deficiencies the
Department Finds
During its Program
Reviews**

Finding

The department's procedures do not ensure that charitable institutions, summer camps, and food processors take prompt corrective action on deficiencies the department notes during its program reviews of these institutions. Specifically, of the 22 charitable institution reviews that we selected for testing, 14 had deficiencies that required follow-up. The department did not establish a due date for corrective action for deficiencies noted during their review of two of the institutions; however, these two institutions did take prompt corrective action. Also, although one of these 22 charitable institutions did not inform the department of its corrective action by the due date established by the department, the department did not take any follow-up action until 145 days after the required due date. Further, the department indicated that it had conducted reviews of all 22 charitable institutions in our sample, but the department could not provide documentation for one of the charitable institution's reviews.

Additionally, we selected 22 summer camp reviews for testing. For one of the 22 summer camps, the department could not provide documentation that it completed a review. Finally, the department noted deficiencies at 5 of the 10 food processors that we reviewed. However, it did not take any follow-up action on one of these 5 processors until 82 days past the date that the department required the processor to provide the corrective action.

Criteria

The Code of Federal Regulations, Title 7, Section 250.19(3), requires that the department provide a report of its program reviews to each institution that it reviews. This report must include recommendations for corrective action and a timetable for completion. Additionally, it requires the department to monitor the completion and the effectiveness of corrective actions.

Recommendation

The department should ensure that it establishes due dates for corrective actions for deficiencies that it notes in the program reviews that it conducts. Additionally, the department should take prompt follow-up action for those institutions that do not provide prompt notification to the department that they have taken the required corrective action. Finally, the department should ensure that it retains documentation of the reviews that it conducts.

**Item 10.
Inadequate
Procedures To
Ensure That Local
Educational
Agencies Comply
With Federal
Regulations**

Finding

The department's procedures do not ensure that instances of noncompliance with federal regulations identified in the audit reports of LEAs are resolved within six months. We found that 13 of 30 audit reports we reviewed identified instances in which the LEA did not comply with federal laws and regulations. For 12 of these 13, the department did not ensure that the LEAs resolved within 6 months the instances of noncompliance with federal laws and regulations identified in these reports.

We reported a similar weakness during our audit for fiscal year 1991-92. In its response to that finding, the department stated that it had developed an action plan to follow up on the audit exceptions in the 1991-92 audit reports as quickly as they are received.

Criteria

OMB Circular A-128 requires that state or local governments that allocate \$25,000 or more of federal financial assistance to an LEA must determine whether the LEA spent the federal financial assistance in accordance with federal laws and regulations. Also, for instances of noncompliance with federal laws and regulations, OMB Circular A-128 requires that state or local governments ensure that appropriate corrective action is taken within six months of receipt of the audit report.

Recommendation

The department should ensure that LEAs correct all instances of noncompliance with federal laws and regulations identified in the audit reports within six months.

**Item 11.
Inadequate
Procedures To
Ensure that
Private, Nonprofit
Agencies Comply
With Federal
Regulations**

Finding

The department does not adequately monitor the audit reports that private, nonprofit agencies submit to the department for the National School Lunch and School Breakfast (NSL&SB) programs.

We found that the department's Office of External Audits (office) did not maintain adequate records to determine which private, nonprofit agencies participating in the NSL&SB programs submitted an audit report for fiscal year 1991-92. Without adequate records, the office cannot ensure that it receives audit reports from all participating agencies. If the office does not receive audit reports from all agencies, it cannot ensure that agencies whose audit reports identified deficiencies have taken corrective action to resolve the deficiencies.

Because the office did not have adequate records, we obtained information to determine which agencies were required to submit audit reports from the department's Child Nutrition and Food Distribution Division. Using this information, we selected 21 audit reports to review, and found that the office could not provide 11 of these reports. Of the 10 reports provided, the office had reviewed only 5.

Additionally, we found that the department could not provide us with Annual Audit Status Certifications (AASC) for the NSL&SB programs. The AASCs, which the department requires all participating agencies to submit, indicate if the agency received more or less than \$25,000 in federal funds. From this, the department can determine the type of audit that is required. The AASC also indicates the reporting period selected by the agency. Without this information, we could not determine if the department properly determined the type of audit that each agency required, nor could we determine when each agency's audit report was due to the department.

We reported a similar weakness during our audit for fiscal year 1991-92. In its response to that finding, the department stated that it would ensure that it can provide a listing of private, nonprofit agencies participating in the NSL&SB programs that are required to submit an audit report through a computerized listing backed up by multiple diskettes. Additionally, the department stated that it would prevent loss of audit reports in the future by building checks and balances into its newly updated database system.

Criteria

According to OMB Circular A-133, state or local governments that allocate \$25,000 or more of federal financial assistance to nonprofit institutions must ensure that the institutions obtain an independent audit that determines whether federal financial assistance was spent in accordance with applicable laws and regulations. Additionally, the circular states that audits shall usually be performed annually, but not less frequently than every two years. Finally, a departmental policy directed to all school nutrition program sponsors requires that private, nonprofit agencies submit annual audit reports and AASCs to the department.

Recommendation

The department should adequately monitor the audit reports submitted by private, nonprofit agencies and ensure that they obtain independent audit reports every year. Additionally, the department should ensure that it obtains AASCs from participating agencies each year.

Item 12.
The Department
Did Not Transfer
Statewide Cost
Allocation Plan
Recoveries Within
30 Days as
Required by the
State Administrative
Manual and the
Government Code

Finding

The department did not promptly transfer to the State's General Fund reimbursements representing the federal government's share of service costs provided by central service agencies. Central service agencies provide services such as financial, personnel, and legal support. These costs are calculated under the Statewide Cost Allocation Plan (SWCAP), which is the plan that each state agency uses to pay for its share of the State's cost for central services. The department transferred the SWCAP recoveries for the periods July through September on December 28, 1992—59 days late; October through December on March 13, 1993—41 days late; January through March on May 24, 1993—24 days late; and April through June on October 25, 1993—87 days late.

The Office of the Auditor General reported a similar weakness during its financial audit for fiscal years 1989-90 and 1990-91. In the departments' response to the finding, it stated that SWCAP recoveries are no longer a problem; however, our audit work showed that the problem still exists.

Criteria

The California Government Code, Section 13332.01, requires agencies to recover SWCAP costs from the federal government. Although no deadline is expressly mandated by the Government Code, the State Administrative Manual, Section 8755.2, implies that a transfer of SWCAP recoveries to the State's General Fund within 30 days of the end of each quarter would be appropriate.

Recommendation

The department should transfer SWCAP recoveries within 30 days.

Item 13.**Failure to Adequately Monitor Local Educational Agencies for the Chapter 1 Programs—Local Educational Agencies and the Federal, State, and Local Partnerships for Educational Improvement (Chapter 2) Programs****Finding**

The department does not always ensure that it performs required on-site reviews of LEAs participating in the Chapter 1 Programs—Local Educational Agencies and the Federal, State, and Local Partnerships for Educational Improvement (Chapter 2) programs. The department performs on-site reviews through its program of Coordinated Compliance Reviews (CCR). We reviewed the department's records for 22 of the CCRs that were required for fiscal year 1992-93 and found that the department failed to conduct one of them. Furthermore, the department also failed to perform a CCR at this same LEA that was required in fiscal year 1989-90. If the department does not perform CCRs when they are required, it cannot ensure that LEAs are complying with federal program requirements.

Criteria

The Code of Federal Regulations, Title 34, Section 80.40(a), requires the State to monitor activities to ensure that subgrantees comply with applicable federal requirements and achieve performance goals. To meet this requirement, the department's CCR program requires that the department conduct an on-site review of each LEA on a three-year cycle.

Recommendation

The department should ensure that it performs CCRs at each LEA as required.

Item 14.**Noncompliance With Other Federal Requirements****Finding and Criteria**

In the following instances, the department did not always comply with administrative requirements of the federal government.

We reviewed 30 applications from LEAs that were funded for participation in the Drug-Free Schools and Communities—State Grants program in fiscal year 1992-93. We found one application that was substantially incomplete, one application that contained inaccurate resources data, three applications that were not received by the department within 120 days from the date that the department sends its entitlement letter as required, and one application that did not contain the required progress report or financial summary.

The United States Code, Title 20, Section 3196, requires that LEAs submit an application and provide information and assurances as the state educational agency responsible for distributing the grant reasonably determines to be necessary. We reported similar weaknesses in our fiscal year 1991-92 audit report.

General Government

Office of Criminal Justice Planning

Our contractor, Gilbert Accountancy, reviewed the Office of Criminal Justice Planning's (OCJP) administration of the U.S. Department of Justice grant, Federal Catalog Number 16.579. There are additional issues at OCJP relating to fiscal years 1991-92 and 1992-93 that have not been resolved. An additional report discussing these issues will be issued later.

Item 1. Expenditures for Equipment Not Authorized in Grant Agreement

Finding

We tested \$397,438 of equipment expenditures for a computer system that were paid with 1992 Drug Control and System Improvement (DCSI) grant funds and determined that the funds were not authorized in the grant agreement. Furthermore, we were unable to obtain documentation of specific authorization for the purchase. We also noted an additional \$445,507 of expenditures for the computer system that were charged to the grant in previous years. In total, the OCJP charged \$842,945 to the DCSI for the computer system. Because it did not specify in its grant agreement the intention to purchase the computer equipment, the OCJP may be liable to the federal government for the unauthorized expenditures.

Criteria

Special Condition 10 of the grant award states that in compliance with Section 623 of Public Law 102-141, no amount of the award shall be used to finance the acquisition of goods unless the recipient specifies in the award contract the amount of federal funds that will be used to finance the acquisition. Special Condition 10 of the grant award also states that this requirement only applies to purchases for goods and services that in aggregate exceed \$500,000.

Recommendation

The OCJP should specifically identify in the grant agreement its intention to purchase goods or services in excess of \$500,000.

Item 2. Subrecipients Are Not Promptly Submitting Financial and Program Reports

Finding

During our review of financial and program reports, we noted that the subrecipients did not promptly submit the reports to the OCJP. As a result, the OCJP did not have the information that it needed to prepare accurate federal quarterly reports for the Drug Control and System Improvement—Formula Grant. For example, during our review, we noted that program income and related expenditures on the quarterly

report for the period ending June 30, 1993, were understated by approximately \$59,000 and \$631,000, respectively. This issue was also raised by the OCJP's internal auditors in its report issued December 1, 1993.

Criteria

Section 10410 of the OCJP Grantee Handbook states that financial and program reports are due 30 calendar days after the end of the reporting period.

Recommendation

To ensure that it has the information that it needs to prepare accurate federal reports, the OCJP should require its subrecipients to promptly submit their financial and program reports.

Item 3. OCJP Not Adequately Monitoring Its Subrecipients

Finding

During our review of the OCJP's procedures to monitor subrecipients, we noted that the OCJP had not monitored the programs at three of the four counties in our sample. In addition, we noted that as of January 25, 1994, nearly seven months after the end of the fiscal year, the OCJP had not received audit reports from two of the four counties in our sample. By not monitoring all of its subrecipients, the OCJP cannot ensure that the programs are operating as prescribed. In addition, if the OCJP does not ensure that counties submit audit reports, the OCJP cannot affirm that subrecipients are using federal funds in compliance with federal guidelines.

Criteria

The OCJP Grantee Handbook, Section 10410, states that all projects will be monitored at least once every three years, or prior to the expiration of the project if the funding cycle is less than three years. The Drug Control and System Improvement—Formula Grant award period for subrecipients is one year; therefore, the OCJP should monitor subrecipients each year.

The OCJP Grantee Handbook, Section 8120, requires grantees to submit audit reports to the OCJP Audits Division no later than six months after the close of the grant period. In addition, the federal Office of Management and Budget (OMB), Circular A-128, Section 13(f), states that audit reports must be submitted to the federal agency that provided federal assistance funds within one year after the end of the audit period. Finally, Section 17 of OMB Circular A-128

states that agencies must consider sanctions that may include withholding a percentage of assistance payments or suspending the federal assistance until the audit is satisfactorily completed.

Recommendation

The OCJP should follow its procedures by monitoring each program annually. In addition, the OCJP should ensure that all subrecipients promptly submit their audit reports to the OCJP Audits Division.

Item 4. Audit Findings Are Not Resolved Within Required Time Frames

Finding

The OCJP has procedures in place to resolve subrecipient audit findings; however, the OCJP is currently backlogged in resolving the findings. According to the Chief of the Audits Branch, the backlog of reports dates back as far as 1989. This backlog may cause several problems such as:

- Due to the time delay, subrecipients may not have the financial capability to repay funds if the OCJP determines that repayment is required;
- Because deficiencies are not resolved on a timely basis, the unfavorable condition may persist in subsequent grant periods; and
- By waiting several years to question transactions, supporting documentation and explanations may be difficult to obtain.

Criteria

Statement of Auditing Standards No. 68, Paragraph 74; the Single Audit Act; and OMB Circular A-128 all require the grant recipient (OCJP) to monitor subrecipients and to take corrective action within six months after instances of noncompliance have been discovered.

Recommendation

The OCJP should reduce the length of time it takes to resolve audit findings. To become current, the OCJP has started subcontracting out the review of audit reports and has restructured its internal audit section. While these changes will make the review process more timely, they do not address the resolution of findings with the subrecipients. The OCJP should continue its efforts to improve its progress in resolving audit findings.

**Item 5.
Approval of
Subrecipient
Application Not
Timely**

Finding

During our review of ten applications that subrecipients submitted to the OCJP requesting funds, one was not approved within 45 days of official receipt. The OCJP's policy is to consider applications approved unless the OCJP notifies an applicant in writing prior to the end of the 45-day period. Since applicants are only notified of disapproval, not approval, this policy could leave an applicant confused about whether its application had actually been approved.

Criteria

The Anti-Drug Abuse Act, Section 508(a), states that each application made by a local unit of government for funds shall be deemed approved no later than 45 days after receipt unless the State notifies the applicant in writing that the application has been disapproved. In addition, the section requires the State to inform the applicant in writing of specific reasons for the disapproval.

Recommendation

The OCJP should ensure that it either approves or disapproves applications that it receives from subrecipients within 45 days of actual receipt.

**Item 6.
Incorrect Deposits
of Federal Funds**

Finding

During our review of cash, we noted that funds drawn down were not consistently deposited under the correct federal catalog number. For example, we noted three instances where funds drawn down for the Juvenile Justice and Delinquency Prevention program (JJDP) were deposited at the State Controller's Office under the catalog number for the Drug Control and System Improvement—Formula Grant (DCSI). We also noted one instance where funds drawn down for the DCSI program were deposited under the federal catalog number for the JJDP program. As a result of these errors, approximately \$148,000 was incorrectly deposited into the DCSI program. According to the Chief of the Accounting Branch, these errors occurred because staff preparing the remittance advices did not verify the federal catalog number with the drawdown documents.

Criteria

The State Accounting Manual, Section 7976, requires agencies to reconcile their revenue and expenditure accounts monthly, within 30 days of the preceding month, with transactions per the State Controller's Office.

**Item 7.
Indirect Cost
Allocation
Procedures Need
Improvement**

Recommendation

The OCJP should reconcile the amount of funds that it draws down to the deposits recorded at the State Controller's Office.

Finding

During our review of the indirect cost plan, including the CALSTARS cost allocation computations and costs reported to the Office of Justice Programs—Bureau of Justice Assistance, we found that expenses for the first six months of fiscal year 1992-93 were recorded into the administrative cost accounts instead of into the appropriate budget categories. This allocation was not in accordance with OMB Circular A-87.

The budget branch did not submit its cost allocation tables to the accounting branch until February 1993, when it should have been in place by July 1992. Costs charged to the budget accounts were not properly allocated for July 1992 through January 1993. These costs were allocated in accordance with the general overhead plan instead of in accordance with the grant budget.

Criteria

OMB Circular A-87 states that costs are allowable for federal reimbursement only to the extent of benefits received by federal programs and costs must meet the basic guidelines of allowability, reasonableness, and allocability.

The State Administrative Manual, Section 9205, requires that any cost allocation procedure adopted by an agency shall provide for auditability. The section also requires that any cost allocation procedure adopted by an agency shall provide for timeliness.

Recommendation

The OCJP should ensure that its cost allocation tables are completed and submitted to the accounting branch within 30 days after the budget is signed by the Governor to allow for costs to be properly allocated. If the tables are late, the OCJP should still ensure that costs are properly allocated in accordance with its Indirect Cost Rate Plan.

Item 8. Delays in Disbursing Federal Monies

Finding

During our review of five requests for funds, we noted that in two instances, it took more than 20 days for the funds to be paid to the subrecipient. In addition, we noted one other instance where it took more than 14 days from the date the funds were drawn down to the date the subrecipients were paid.

Criteria

The Code of Federal Regulations, Title 31, Section 205.4(a), requires that the timing and amount of federal cash advances be as close as administratively feasible to the actual disbursement by the recipient organization.

Recommendation

The OCJP should ensure that its requests for federal funds are limited to its immediate cash needs. In addition, the OCJP should minimize the time between the receipt of federal funds and actual disbursement of such funds to its subrecipients.

Item 9. Allocation of Salaries Is Not Sufficiently Documented

Finding

The OCJP was unable to provide sufficient documentation to support the allocation of salaries between the DCSI grant and other grants administered by the Anti-Drug Abuse Branch. As a result, the OCJP cannot demonstrate that the costs allocated are equitable relative to the benefits the programs receive.

Criteria

OMB Circular A-87 requires that direct costs charged to federal grants be necessary and reasonable to administer the grant and that costs should be allocated to grant programs in accordance with the benefits received.

Recommendation

The OCJP should develop a procedure to allocate salaries among various grants that the Anti-Drug Abuse branch administers. This allocation could be determined using either a time study or by prorating staff time based upon the percentage of time spent administering the DCSI grant.

Department of Economic Opportunity

We reviewed the Department of Economic Opportunity's (department) administration of the U.S. Department of Health and Human Services grants, Federal Catalog Numbers 93.568 (formerly 93.028) and 93.569 (formerly 93.031).

Item 1. Improper Payment to a Service Provider

Finding

The department improperly issued a payment advance to a service provider with which it did not have an approved contract. As a result, it unnecessarily risked state and federal funds. In this instance, the department issued a payment advance on January 17, 1992, and finalized the contract on February 28, 1992. The department made the improper payment because it did not use the normal claims processing procedure, through which it would have learned that it did not have an approved contract with the service provider. Instead, the department issued the payment through its revolving fund. Department staff were not certain why, in this instance, the department did not make the payment through the normal claims processing procedure and issue a warrant through the State Controller's Office.

Criteria

Section 8110 of the State Administrative Manual states that revolving fund checks are to be used for the payment of compensation earned, travel expenses, travel expense advances, or when immediate payment is otherwise necessary. Section 8110 further states that when determining whether immediate payment is necessary, the determining factor is whether payment could be made through the normal claim processing procedure and a State Controller's Office warrant issued.

Corrective Action

According to the department's director, it is the department's current policy to issue revolving fund checks to service providers only in emergency situations. The department defines emergency situations as instances when the service provider is unable to meet its payroll. Requests to issue a revolving fund check must be made in writing and must include a justification for the payment. Also, a department deputy director must approve these requests. The director also stated that, since the department implemented the policy, it has issued only four revolving fund checks to service providers and, in each case, the service provider had an approved contract with the department.

Recommendation

The department should continue to comply with its policy of issuing revolving fund checks to service providers only in emergency situations.

Department of Finance

We assessed the compliance of the Department of Finance (department) with federal and state regulations in administering the Statewide Cost Allocation Plan (SWCAP) and with state regulations in administering the Prorata Allocation Plan (prorata).

The SWCAP is the plan each state agency uses to obtain federal reimbursement for the federal government's share, if any, of the State's costs for central services. The federal money is paid into the State's General Fund. The prorata is the plan that each state agency uses to obtain reimbursement from its special funds for the special funds' share, if any, of the costs for central services. The money from the special funds is also paid into the State's General Fund.

Eleven executive agencies reporting to the governor, the Department of Justice, the Legislature, the Bureau of State Audits (formerly the Office of the Auditor General), the State Controller's Office (SCO), the State Library, and the State Treasurer's Office, provide various central services to state agencies. These entities, called "central service agencies," provide services such as financial, personnel, and legal support. (Attachment A lists the agencies performing central services during fiscal year 1992-93 and identifies the three agencies we reviewed.)

The department allocates the costs of the SWCAP to the federal government and the costs of the prorata to the State's special funds based on costs and workload data from the central service agencies and from the governor's budget. Initially, central service costs are paid from the State's General Fund, and then, the amounts allocated to and paid by the federal government and the special funds are transferred to the State's General Fund. (Attachment B shows the estimated SWCAP and prorata expenditures and recoveries for fiscal year 1992-93.)

Item 1. Noncompliance With Certain Federal and State Requirements

Finding and Criteria

- The department made several errors in calculating the workload data for fiscal year 1992-93 affecting its Legislation and Intergovernmental Relations Unit for 12 agencies, its Corrections/Judicial Unit for 2 agencies, its Business, Transportation, and Housing Unit for one agency, its Health and Welfare Unit for 2 agencies, and its Budget Operation Support Unit for 3 agencies. In addition, the department made four errors in

allocating workload hours within 3 agencies in the Health and Welfare Unit. The cumulative effect of these errors was a 19.5 hour understatement of the department's workload. The Office of the Auditor General reported a similar weakness during its audits for fiscal years 1987-88 through 1990-91. In its audit response dated May 19, 1992, the department stated that it had developed a time reporting system for the budget units which should improve the recordkeeping and control of this function. The federal Office of Management and Budget, Circular A-87, states that federal programs should bear their fair share of costs recognized under Circular A-87.

- The department made an error in compiling expenditure data for a central service function of the State Controller's Office (SCO). The department overstated the SWCAP and prorata expenditures for the SCO field audits function by \$90,000. This error could result in the overcollection from the federal government of approximately \$7,000 and overcollection from the State's special funds of approximately \$34,000. The federal Office of Management and Budget, Circular A-87, requires the State to charge the federal government only for allowable costs. In addition, the State Administrative Manual, Section 8752, requires state agencies to recover full costs for goods or services provided for other state agencies.

Recommendation

The department should improve its compliance with these federal and state requirements.

ATTACHMENT A

AGENCIES PERFORMING CENTRAL SERVICES
FISCAL YEAR 1992-93

<u>Agency Name</u>	Reviewed by the Bureau of <u>State Audits</u>
Department of Finance	X
Department of Justice	
Department of Personnel Administration	
Health Benefits for Retired Annuitants (administered by the Public Employees' Retirement System)	X
Legislature	
Office of Administrative Law	
Bureau of State Audits/Office of the Auditor General	
Business, Transportation and Housing Agency	
Health and Welfare Agency	
Resources Agency	
State and Consumer Services Agency	
Youth and Adult Correctional Agency	
State Board of Control	
State Controller's Office	X
State Library	
State Personnel Board	
State Treasurer's Office	

ATTACHMENT B

**ESTIMATED SWCAP AND PRORATA
EXPENDITURES AND RECOVERIES
FISCAL YEAR 1992-93
(In Millions)**

Estimated SWCAP expenditures	\$419.1
Estimated SWCAP recoveries from the federal government	\$ 32.3
Percent of estimated recoveries	7.7%
Estimated prorata expenditures	\$489.4
Estimated prorata recoveries from the State's special funds	\$185.0
Percent of estimated recoveries	37.8%

Source: State of California, Department of Finance

Military Department

We reviewed the Military Department's controls over materials used for building repairs and reviewed pertinent inventory records at the Directorate of Facilities Engineering at Camp Roberts.

Item 1. Control Weaknesses Over Materials Used for Building Repairs

Finding

The Military Department had inadequate controls over materials used for building repairs at the Directorate of Facilities Engineering (DFE) at Camp Roberts.

The following is a list of the control weaknesses we identified:

- The DFE's Supply Section issued materials to employees even when they did not properly identify the specific work projects for which the materials were needed.
- The Supply Section supervisor sometimes wrote off materials that were unaccounted for in the inventory by using the requisition forms to record the missing materials as assigned to other divisions.
- In numerous instances, Supply Section staff found substantial materials that were unaccounted for in various locations at Camp Roberts. The Supply Section supervisor subsequently added these found materials to the supplies inventory.
- Workshop staff do not account for materials issued to the various workshops. These materials are often issued to workshops in large quantities, such as 100 sheets of plywood.
- The DFE does not reconcile the materials issued by the Supply Section and the materials used in the various work projects. Moreover, when materials are unused on one work project, they are sometimes used on another project without any record of the transfer.
- There is insufficient segregation of duties in the Supply Section. Specifically, the Supply Section supervisor could issue and write off materials from the supplies inventory as well as make other adjustments to the inventory records.

Because of these weaknesses, the DFE cannot be certain that materials are properly used and that they are not misappropriated for personal gain.

Criteria

The California Government Code, Sections 13402 and 13403, requires state offices to ensure that a satisfactory system of internal and administrative controls is in place to provide effective controls over assets, liabilities, revenues, and expenditures.

Recommendation

The DFE should correct the control weaknesses described above to ensure that materials used for building repairs are adequately safeguarded.

Health and Welfare

Department of Aging

We reviewed the Department of Aging's (department) administration of the U.S. Department of Agriculture grant, Federal Catalog Number 10.550, and the U.S. Department of Health and Human Services grants, Federal Catalog Numbers 93.044 (formerly 93.633) and 93.045 (formerly 93.635).

Item 1.

Inaccurate Federal Financial Reports

Finding

The department overstated federal expenditures for the Title III grant for federal fiscal year 1993. Specifically, for the period July 1, 1993 through September 30, 1993, the department overstated federal expenditures for the Title III grant by \$884,968. This error occurred because an adjustment for area administration was not properly reflected in the worksheet used to prepare the financial status report. On the worksheet, federal expenditures for area administration were increased by \$442,484 when they should have been decreased by this same amount. As a result, the federal expenditures for the grant were overstated by \$884,968. After we informed the department of the error, the department corrected it. In addition, when the department submitted its final status report for the 1993 grant it properly reflected the amount of federal expenditures for area administration.

Criteria

The Code of Federal Regulations, Title 45, Section 74.61 (a) requires the department to submit accurate, current, and complete financial reports.

Recommendation

The department should ensure that financial reports it submits to the federal government in the future contain accurate and reliable information.

Item 2.

Failure To Monitor Area Agencies' Programs To Provide Supportive and Nutrition Services

Finding

The department did not conduct performance evaluations of all the area agencies on aging. Specifically, the department did not conduct annual on-site performance evaluations of their supportive services for 17 of the 33 area agencies during fiscal year 1992-93. In addition, the department did not conduct on-site performance evaluations of the nutrition services for 20 of the 33 area agencies during the past two

fiscal years. Failure to conduct these evaluations may prevent early detection and correction of irregularities or deficiencies in the services that the area agencies provide.

According to the Deputy Director of the Long-Term Care and Aging Services Division, the department was not able to conduct the monitoring visits because of budget concerns, workload demands of other projects and staff vacancies in the Nutrition Section. In addition, she stated that the department performs many other tasks that assist in assuring compliance with federal laws and regulations. Specifically, the department reviews the area agencies' annual plans, and regularly reviews management information compiled from the program operations data submitted to the department by the area agencies.

Criteria

The Code of Federal Regulations, Title 45, Section 1321.11(a) and (b), requires the department to develop policies for monitoring the performance of programs and activities initiated to provide supportive and nutrition services under Title III of the Older Americans Act. The department's Title III Program Manual, Section D, paragraph 43.1(g) requires the department to conduct on-site performance evaluations of the supportive services of the area agencies annually. In addition, the department's goal is to conduct on-site evaluations of the nutrition services of area agencies at least every two years.

Recommendation

The department should conduct on-site evaluations of the supportive services of all area agencies annually and on-site evaluations of the nutrition services of all area agencies at least every two years.

Department of Alcohol and Drug Programs

We reviewed the Department of Alcohol and Drug Programs' (department) administration of the U.S. Department of Education grant, Federal Catalog Number 84.186, and the U.S. Department of Health and Human Services grants, Federal Catalog Numbers 93.959 and 93.992.

Item 1. Failure To Adequately Monitor Cash Reports

Finding

The department does not have adequate procedures to monitor the cash balances of subrecipients of the Alcohol and Drug and Mental Health Services/Substance Abuse Prevention and Treatment (ADMS/SAPT) block grant and the Drug-Free Schools and Communities—State Grants (DFSC). During our review of quarterly reports for 33 counties, we found that 6 of the counties reported cash balances that would last more than 30 days. Furthermore, we determined that the department did not withhold or adjust subsequent monthly advances for any of these 6 counties. Finally, we determined that 10 of the counties submitted their reports late and one report was missing.

Without adequate procedures to monitor cash balances of subrecipients, the department cannot be sure that it limits monthly cash advances to the minimum and immediate needs of the subrecipients. Consequently, the State may be advancing federal funds to subrecipients before they need the money. If the department fails to limit cash advances to minimum and immediate needs, it could jeopardize future advances of federal grant funds.

The Office of the Auditor General reported similar weaknesses in its reports for fiscal years 1989-90 through 1991-92. In its May 28, 1992, response to the fiscal year 1990-91 report, the department indicated that during fiscal year 1992-93, it would implement procedures for monitoring subrecipients' cash balances and for advancing them money for federally-funded programs.

Criteria

The Code of Federal Regulations, Title 31, Section 205.4 (a), requires that cash advances to a primary recipient be limited to the minimum amounts needed and be timed in accord with only the actual, immediate cash requirements of the recipient. The timing and amount of cash advances must be as close as is administratively feasible to the actual disbursements by the recipient for direct program costs and the proportionate share of any allowable indirect costs. In addition,

Section 205.4(e) requires that advances by primary recipients to subrecipients conform substantially to these same standards of timing and amount. Finally, the California Government Code, Section 13401, requires agencies to ensure that a satisfactory system of internal controls is in place to provide effective accounting control over assets, liabilities, revenues, and expenditures.

Recommendation

The department should review quarterly cash reports to determine whether it needs to adjust cash advances to subrecipients so that cash on hand is limited to amounts required for immediate needs. In addition, the department should ensure that the subrecipients promptly submit the quarterly cash reports to the department.

Item 2. Inadequate Monitoring of an Interagency Agreement for the Drug Free Schools and Communities Grant

Finding

The department did not adequately monitor its interagency agreement with the Office of Criminal Justice Planning (OCJP). The interagency agreement provided funds from the DFSC grant to the OCJP to support various drug abuse education and prevention programs. During our review of the payment ledgers for the interagency agreement, we determined that as of December 1993, more than two months after the end of the agreement period, approximately \$678,000 of the \$927,667 that the department advanced to the OCJP was outstanding. After we notified the department of the outstanding balance, it applied additional claims that the OCJP submitted to the department for reimbursement to reduce the outstanding balance; however, as of February 17, 1994, the outstanding balance still exceeded \$369,000. Because the department did not adequately monitor the interagency agreement, it cannot ensure that the funds it advanced to the OCJP were limited to its minimum and immediate cash needs.

Criteria

The interagency agreement requires the OCJP to submit invoices to the department for services performed under the agreement. In addition, the interagency agreement requires the OCJP to repay all funds advanced to it during the contract period. Further, the interagency agreement states that if the OCJP does not repay the advance prior to the end of the agreement, the department must take action to recover the advance. Specifically, the agreement states that during the last three months of the agreement period, the department must apply all claims that the OCJP submits for reimbursement to the outstanding balance of funds advanced to the OCJP. Finally, the Code of Federal Regulations,

Title 31, Section 205.4(e), requires that cash advances from primary recipients to subrecipients be limited to the minimum and immediate needs of the subrecipient.

Recommendation

The department should monitor its agreements with OCJP to ensure that either the OCJP repays the department for the funds advanced, or the department recovers the funds advanced prior to the end of the agreement period.

Item 3. Incorrect Allocation of Costs for Audit Services

Finding

The department did not comply with its cost allocation plan. Specifically, during our review of the rates used to allocate the costs for audit services, we determined that the rates in the cost allocation plan did not match the rates in the department's accounting system. The cost allocation plan required the department to allocate the costs for audit services to six program cost accounts (PCAs) at rates ranging from 4.038 percent to 30 percent. However, we determined that the department's accounting system allocated costs for audit services to only four of the six PCAs. Further, we determined that the department allocated 25 percent of the costs for audit services to each of the four PCAs. Finally, we determined that the four PCAs the department allocated the costs to were supported with state funds, while the two PCAs for which the department did not allocate costs were supported with federal funds. Because audit services benefit both state- and federally-funded programs, the incorrect allocations resulted in an overstatement of approximately \$14,000 in expenditures of state funds and, conversely, an understatement of the same amount of expenditures from the Federal Trust Fund.

Criteria

The Code of Federal Regulations, Title 45, Subtitle A, Part 92, Section 92.22 and Title 34, Subtitle A, Part 80, Section 80.22 require that allowable costs be determined by using the cost principles contained in the Office of Management and Budget (OMB) Circular A-87. Circular A-87 states that costs should be allocated to grant programs in accordance with the benefits received.

Recommendation

The department should ensure that administrative costs are allocated in accordance with federal cost principles as outlined in the OMB Circular A-87. In addition, the department should allocate administrative costs in accordance with its own cost allocation plan.

Employment Development Department

We reviewed the financial operations and related internal controls of the Employment Development Department (department) and the department's administration of the U.S. Department of Labor grants, Federal Catalog Numbers 17.207, 17.225, 17.246, and 17.250; and the U.S. Federal Emergency Management Agency grant, Federal Catalog Number 83.516.

**Item 1.
No Procedures
To Ensure
Subrecipients
Submit Audit
Reports Within
Required
Timeframes**

Finding

The department has not established procedures that outline actions it will take when subrecipients of the Job Training Partnership Act (JTPA) grant do not submit audit reports within 13 months after the end of the State's fiscal year. The department is responsible for monitoring the private nonprofit subrecipients of JTPA funds. We selected for review eight nonprofit subrecipients to see when their audit reports were submitted. We found that two audit reports have not been submitted to the department's audit division and one of the reports was submitted more than 13 months after the end of the State's fiscal year. If the audit division does not receive audit reports within 13 months after the end of the State's fiscal year, it may not be notified of major instances of noncompliance with federal laws and program regulations. Thus, the department may be delayed in implementing corrective action.

We reported a similar weakness during our financial audit of fiscal year 1991-92. The department responded that it would prepare written procedures that outline the steps it will take when a subrecipient does not submit an audit report within the time requirements established under federal law.

Criteria

The Office of Management and Budget (OMB), Circular A-133, Section 15(i), requires that audit reports be submitted no later than 13 months after the end of the State's fiscal year.

Recommendation

The department should ensure that subrecipients submit audit reports within the federally-required timeframe.

**Item 2.
Late Resolution of
Audit Reports**

Finding

In fiscal year 1992-93, for 5 of the 72 JTPA subgrantees' audit reports, the department did not issue audit resolution final determination letters within six months after the department's audit division received the final audit report. Failure to resolve questioned costs and administrative findings can result in additional questioned costs if the subgrantees do not correct deficiencies in their internal controls within a reasonable time.

The Office of the Auditor General reported a similar weakness during its financial audits for the eight previous fiscal years. In fiscal year 1991-92, we saw improvement in the number of audit reports resolved late. For fiscal year 1991-92, the department was late in resolving 11 of 81 audit reports.

Criteria

OMB Circular A-128, Section 14, and Circular A-133, Section 16(b), require the department to make an audit resolution determination within six months after receipt of the audit report and to proceed with corrective action as soon as possible.

Recommendation

The department should continue its efforts to reduce delays in the resolution of audits so it can resolve questioned costs and administrative findings in all subgrantees' audit reports within the required timeframe.

**Item 3.
Insufficient
Monitoring of
Subrecipients' Cash
Balances**

Finding

The department does not have documentation to show that it properly monitored the cash balances of its JTPA program subrecipients. Although the department requires its subrecipients to submit monthly status of cash reports, we identified the following weaknesses:

- The Fiscal Programs Division (FPD) did not always follow its own procedures when there was a problem with the monthly status of cash reports. The FPD's procedures require that monthly reports from subrecipients that show excess cash be forwarded to the Job Training Partnership Division (JTPD) for further action. For two of the 24 cases we reviewed, the FPD did not forward the reports with excess cash to the JTPD for further action. In addition, if the FPD forwards a case to the JTPD for follow-up and the FPD does not receive a response from the JTPD within 30 days, the FPD's procedures require it to communicate with the JTPD to determine

the status of the case. Four of the 24 cases we reviewed were forwarded to the JTPD for follow-up. However, JTPD did not take any action for 6 to 13 months after receiving the cases from FPD. When JTPD followed-up on the cases, it was able to determine that no excess cash problems existed.

- The JTPD does not have a system to ensure proper action is taken when monthly status of cash reports are referred to them by the FPD. In addition, the JTPD does not maintain records indicating which monthly status of cash reports were received from the FPD. Therefore, the JTPD is unable to adequately monitor the status of these reports.
- The JTPD does not enforce its requirement that subrecipients maintain interest-bearing accounts for JTPA funds and remit interest earnings quarterly to the department. According to a list provided by the department, only 33 of the 52 subrecipients maintain JTPA funds in interest-bearing accounts and remit them to the department. Since the amount of interest that these 33 subrecipients submitted to the department for fiscal year 1992-93 totaled approximately \$100,000, it appears that the interest earnings not remitted by the other 19 subrecipients could be significant.

We reported similar weaknesses during our financial audit of fiscal year 1991-92. The department responded that the FPD is developing procedures to ensure that subrecipients are contacted to resolve incorrect monthly status of cash reports. In addition, the JTPD is developing a tracking system to follow the resolution of excess cash reviews. Further, the department responded that it is reviewing the requirement that subrecipients maintain JTPA funds in separate interest-bearing accounts.

Criteria

The Code of Federal Regulations, Title 31, Section 205.4(a), requires that cash advances to primary recipients be limited to minimum amounts needed and be timed in accordance with the actual, immediate cash requirements of the recipient in carrying out the purpose of the approved program or project. The Code of Federal Regulations, Title 31, Section 205.4(e), requires that advances made to secondary recipients are to conform substantially to the same standards of timing and amounts as apply to federal advances to primary recipients.

The FPD's Monthly Status of Cash Review Procedures require that the FPD refer excess cash problems to the JTPD. Furthermore, if the FPD does not receive a response from the JTPD within 30 days regarding the resolution of the problem, the FPD is required to follow-up with the JTPD.

The Job Training Partnership Act, Directive 86-5, requires that all subrecipients shall account for interest earned on advances of JTPA funds separately, maintain an interest-bearing account, and remit the interest earnings to the department quarterly.

Recommendation

The department should improve its compliance with the federal requirements and its own established procedures. Also, the department should develop a system to monitor the status of these reports. Finally, for fiscal year 1992-93, the department should determine if any of the subrecipients not remitting interest, earned interest income on JTPA funds and collect the interest from the subrecipients.

Item 4. Relevant Sections of Federal Expenditure Report Do Not Reconcile

Finding

Throughout fiscal year 1992-93, the department did not properly reconcile or explain two sections of its quarterly report showing the expenditures of federal funds for unemployment compensation paid to federal employees and ex-service members. For example, for the quarter ending June 30, 1993, the difference between the two sections totaled more than \$2 million. Further, the department did not explain the difference as required in the report.

The quarterly report is a summary of expenditures charged to federal unemployment programs for unemployment compensation paid to federal employees and ex-service members. Section A of the report summarizes total expenditures charged to the federal agencies for the quarter. Section B should provide detail of the same total, broken down by charges to each individual civilian and military agency for the quarter. Therefore, the total of the expenditures reported in Section A should equal the total expenditures reported in Section B. In November 1992, the department expected its completion of a new data processing system to resolve reconciliation problems. The new data processing system was completed; however, it did not resolve the problem. Failure to properly assign expenditures in the federal report may result in overcharges or undercharges to certain federal agencies. In addition, charges not properly assigned to federal agencies may

affect the cash solvency of the federal fund that reimburses the State for unemployment compensation benefits paid to federal employees and ex-service members.

We reported a similar weakness during our financial audit of fiscal year 1991-92. The department responded that a work group will develop procedures to identify expected differences between Section A and Section B.

Criteria

The United States Department of Labor's Employment Security Manual, Part V, Section 9336(D)(3), requires that the report totals assigned to federal agencies in Section A be equal to the totals generated from the assigned charges in Section B.

Recommendation

The department should proceed with its work group so that it can submit its report free of any differences between the two sections of the report. Until the report is reconciled, the department should identify the reason for any differences in the report.

Item 5. Noncompliance With Prompt Payment Standards for Unemployment Benefits

Finding

For the 12 months ending March 31, 1993, the department did not comply with federal prompt payment standards for first-time payments of unemployment benefits for interstate claims. On average, the department promptly paid only 47 percent of first-time unemployment benefit payments for all interstate claims. The federal prompt payment standard is 70 percent.

We reported a similar weakness during our financial audit of fiscal year 1991-92. The department responded that it was conducting weekly meetings to identify problems and to ensure that first-time payment requirements are met.

Criteria

The Code of Federal Regulations, Title 20, Section 640.5, requires that, on an annual basis, the State must pay at least 70 percent of all first-time interstate claims within 14 days following the end of the first compensable week of unemployment.

Item 6.
Noncompliance
With Certain State
and Department
Requirements

Recommendation

The department should ensure that first-time unemployment benefit payments are made promptly in compliance with federal regulations.

Finding and Criteria

In the following instances, the department did not always comply with administrative requirements of the State and department:

- In one of the two Wagner-Peyser contracts reviewed for the Employment Service Program, the department did not comply with contract provisions. Although total contract expenditures did not exceed the contract balance, two line items of expense exceeded the amount allowable by \$1,780. Contract provisions require a contract amendment when line items of expense exceed the allocation by more than 10 percent.
- For 2 of the 32 unemployment insurance benefit payments we reviewed, the department could not locate the Continued Claim Form. As a result, we could not compare the endorsement on the warrant with the claimant's signature on the Continued Claim Form. In addition, we could not determine if the claimant signed the Continued Claim Form on or after the applicable week ending date. The State Administrative Manual, Section 1667, describes record retention criteria.

Although individually these instances of noncompliance may appear to be insignificant, they do represent noncompliance with state regulations and noncompliance with department regulations, which are designed to protect the public's resources from abuse.

Recommendation

The department should improve its compliance with each of the state and department requirements.

Health and Welfare Agency Data Center

We reviewed the financial operations and related internal controls of the Health and Welfare Agency Data Center (data center).

**Item 1.
Possible Liability
to the Federal
Government**

Finding

The data center has a possible liability to the federal government estimated to be as much as \$8.6 million for profits it has accumulated in its Health and Welfare Agency Data Center Revolving Fund (revolving fund) between July 1, 1984, and June 30, 1993. The data center's revolving fund is an internal service fund that accounts for centralized electronic data processing services to state agencies. The data center has charged these agencies more than its costs for providing services. In turn, state agencies have passed these charges on to federal programs. The revolving fund accumulates profits when the data center's charges for services exceed its costs. Federal regulations prohibit the State from charging federal programs for more than its costs.

In 1984, the federal Department of Health and Human Services (DHHS) audited the State's rate-setting methods for internal service funds. As a result of the audit, the State was required to refund to the federal government approximately \$14.9 million of the profits accumulated in internal service funds. This amount represented the federal share of profits accumulated in five of the State's internal service funds from July 1, 1969, to June 30, 1984. The federal DHHS and the state Department of Finance agreed that 57.8 percent of the revolving fund's accumulated profits of approximately \$5.1 million at June 30, 1984, resulted from charges to federal programs and, thus, the revolving fund owed the federal government approximately \$3 million.

Currently, the federal DHHS is conducting an audit of the State's rate-setting methods for internal service funds for the period July 1, 1984, through June 30, 1991. As of April 30, 1994, the federal DHHS has not issued its final audit report.

In 1992, the data center estimated the federal share of accumulated profits to be approximately 38 percent of accumulated profits. We did not verify the accuracy of the estimate. Using the same ratio of 38 percent, we estimate that, under current federal regulations, the State may owe the federal government approximately \$8.6 million.

However, an October 1988 proposed amendment to the federal Office of Management and Budget (OMB) Circular A-87, would allow state agencies a reasonable working capital reserve of 60 days' worth of cash expenditures. This amendment, if approved, may further reduce the liability to the federal government.

During our audit, we found that the federal DHHS Division of Cost Allocation authorized a request from the State of Oregon to retain a 60-day working capital reserve, even though the revisions to OMB Circular A-87 have not been finalized. In January 1994, the State of California requested a similar authorization to retain a working capital reserve of 60 days' worth of cash expenditures. However, according to correspondence dated May 6, 1994, the federal DHHS Division of Cost Allocation will not respond to the State's request until the current federal audit is completed.

The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92 and the Office of the Auditor General reported a similar finding during its audits for the fiscal years 1988-89 through 1990-91. The state auditor and the auditor general recommended that the Department of Finance ensure state agencies comply with federal regulations. In his response of December 24, 1993, the director of the Department of Finance stated that, in some cases, state laws and regulations differ from those of the federal government and that the State is working with the federal government to minimize the differences. He stated that guidelines will be developed as soon as such differences are resolved.

Criteria

OMB Circular A-87, "Cost Principles for State and Local Governments," does not allow the State to charge federal programs for amounts that exceed costs. In addition, the California Government Code, Section 13070, provides the Department of Finance with general powers of supervision over all matters concerning the financial and business policies of the State.

Recommendation

The data center should comply with OMB Circular A-87 when establishing billing rates for charges to state agencies receiving federal support. Further, the Department of Finance should ensure that the data center complies with federal regulations. For example, compliance could be ensured by developing guidelines for the data center and state agencies receiving services from the data center. In addition, the

Department of Finance should monitor the proposed amendment to OMB Circular A-87 to determine the effects the amendment may have on state charges to federal programs.

Department of Health Services

We reviewed the financial operations and related internal controls of the Department of Health Services (department) and the department's administration of the U.S. Department of Agriculture grant, Federal Catalog Number 10.557, and the U.S. Department of Health and Human Services grants, Federal Catalog Numbers 93.566 (formerly 93.026), 93.778, and 93.994.

Item 1. Inaccurate Financial Reports

Finding

The department did not accurately prepare its financial reports for fiscal year 1992-93 for its General Fund, Cigarette and Tobacco Products Surtax Fund-Health Education account, and Health Care Deposit Fund. During our audit, we noted the following conditions:

- The department did not accrue all receivables due to its Health Care Deposit Fund at June 30, 1993. In addition, the department did not analyze its accounts receivable balance to identify the amounts it expected to collect in the ensuing 12 months. Because it did not properly accrue and analyze its receivables, the department understated its accounts receivable and overstated its expenditure balances by approximately \$118 million.
- The department did not accurately analyze and report its encumbrances at June 30, 1993, in two departmental funds for which we reviewed encumbrances. Encumbrances represent goods and services ordered but not received by June 30. For its General Fund and Cigarette and Tobacco Products Surtax Fund-Health Education Account, the department overstated its encumbrances by more than \$20 million and \$4.9 million, respectively.
- The department also understated its due to other governments and expenditure accounts in its General Fund because it did not accrue approximately \$2.8 million for the AIDS Drug Assistance program. Additionally, the department overstated these same accounts by approximately \$2.5 million because it accrued invoices that had already been paid.

- Finally, the department incorrectly included claims that had already been paid in its General Fund revolving fund adjusting entry at year end. As a result, the department understated its cash and claims filed accounts by approximately \$495,000.

Failure to accurately analyze and report financial information submitted to the State Controller's Office reduces the ability of the State Controller's Office to prepare the State's financial statements accurately and in accordance with generally accepted accounting principles.

The Bureau of State Audits reported a similar weakness during its audit for fiscal year 1991-92.

Criteria

The State Administrative Manual, Section 8776.2, requires the department to record as valid receivables all receivables which are due and payable and, at June 30, to accrue those abatements that were not previously billed or accrued but which are expected to be collected within the ensuing year. Section 10544 requires agencies to analyze their encumbrances to determine which are valid as of June 30 of each fiscal year. Additionally, Section 10544 also requires agencies to record all valid obligations and expenditures at June 30 that had not been otherwise recorded by that date. Finally, the California Government Code, Section 13403(a)(3), states that the elements of a satisfactory system of internal accounting and administrative control should include, but are not limited to, a system of authorization and recordkeeping procedures that effectively control assets, liabilities, revenues, and expenditures.

Recommendation

The department should ensure that its financial reports are complete and accurate.

Item 2. Unamended Indirect Charges

Finding

For fiscal year 1991-92, the Bureau of State Audits reported that the department had submitted a Cost Allocation Plan (CAP) to the federal Department of Health and Human Services for its approval. Although the CAP was rejected, the department allocated its indirect costs to its federal programs for fiscal year 1991-92 and 1992-93 based on the CAP. Subsequent to the audit, in October 1993, the department did submit and receive approval of an Indirect Cost Rate Proposal (ICRP) for fiscal year 1991-92 and, in April 1994, approval of its 1992-93

ICRP. However, during our audit for fiscal year 1992-93, we saw little evidence that the department had amended indirect charges to agree with the approved rates included in the ICRP. According to the Chief of the Accounting Section, the department plans to adjust the indirect costs charged for the fiscal years 1991-92 and 1992-93 at the closeout of each federal program, when possible, to agree with rates in the approved ICRP.

Criteria

The federal Office of Management and Budget (OMB) Circular A-87, requires the department to prepare a plan for the allocation of costs required to support the distribution of any joint costs related to the grant program. Circular A-87 also states that the department's cognizant federal agency will approve the allocation plan.

Recommendation

The department should ensure that it adjusts its indirect costs for each federal program to agree with the rates approved in the ICRP.

Item 3. Weaknesses In Controls Over Receivables

Finding

The department did not follow procedures that the State Administrative Manual requires to account for and collect receivables related to the Medicaid Drug Rebate Program. According to the department's records at June 30, 1993, these receivables totaled approximately \$239 million. We found the following specific deficiencies:

- The department did not maintain appropriate separation of duties. The employee who mailed the invoices and recorded the invoiced amounts in the accounts receivable ledger also received, deposited, and recorded the invoiced remittances. Failure to maintain proper separation of duties can result in errors and irregularities that may go undetected.
- The department did not have policies or procedures for monitoring and collecting accounts receivable. Without adequate procedures for monitoring and collecting accounts receivable, the department increases the risk that some receivables will become uncollectible.
- The department did not perform a monthly reconciliation between the subsidiary accounts receivable ledger and the general ledger account. Without properly prepared reconciliations, the department lacks assurance that the transactions have been properly recorded and that the financial records are complete.

The Bureau of State Audits reported a similar weakness in its audit for fiscal year 1991-92.

In March 1993, in a response to the department's Internal Audit Division, and again in November 1993, in response to an audit report submitted by federal auditors, the department agreed with similar findings and stated that the establishment of an effective and proper accounts receivable system was a department priority. The department has begun to implement proper accounts receivable procedures related to the Drug Rebate Program. The department increased staff which allowed for better separation of duties. Currently, the department is beginning to monitor and investigate long-outstanding receivables, in addition to reconciling the subsidiary accounts to the general ledger.

Criteria

The California Government Code, Sections 13402 and 13403, requires agencies to ensure that a satisfactory system of internal accounting and administrative control, including a system of authorization and recordkeeping procedures, is in place to provide effective accounting control over assets, liabilities, revenues, and expenditures. More specifically, the State Administrative Manual, Section 8080, states that, preferably, no books of original entry concerning cash receipts, cash disbursements, or invoices should be kept by employees assigned to receive and deposit remittances. Additionally, Section 7800 requires subsidiary ledgers to be reconciled with the general ledger each month. Finally, Section 8776.6 states that each department will develop collection procedures that will assure prompt follow-up on receivables.

Recommendation

The department should continue to develop and implement a comprehensive policy for monitoring and collecting accounts receivable.

Item 4. Insufficient Monitoring of Audit Reports for Nonprofit Subrecipients

Finding

The department did not sufficiently monitor the audit reports of nonprofit subrecipients participating in the Maternal and Child Health Services Block Grant program. We selected for review 24 audit reports that subrecipients should have submitted to the department and found the following:

- The department was not able to provide us with nine of the audit reports we selected for review. Of the 14 audit reports it did submit to us, none were submitted within the department's contractual

deadline and only 12 were submitted within the federal deadlines. The remaining one nonprofit subrecipient that had not submitted an audit report was granted an extension. Without these audit reports, the department lacks assurance that the nonprofit subrecipients are complying with federal laws and regulations.

- The data base list the department uses to monitor the receipt of the required reports for the grant is incomplete. The list did not include seven nonprofit subrecipients. As a result, we could not conclude that the department properly monitored the receipt of the required reports.
- The department did not review 12 of the 14 reports it had received within the required six months. Without prompt review of the reports, the department cannot ensure that it resolves audit findings within the required time frame.

The Bureau of State Audits reported a similar weakness regarding the late submission of audit reports during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness during its audits for fiscal years 1989-90 and 1990-91.

Criteria

The contractual agreements between the State and nonprofit subrecipients establish a deadline of 5 months and 15 days after the end of the subrecipient's fiscal year for the submission of the required audit reports. OMB Circular A-133, which describes audit requirements for nonprofit agencies, requires the State to ensure that its nonprofit subrecipients submit audit reports no later than 13 months after the end of the subrecipients' fiscal year. Circular A-133 also requires the State to resolve audit findings within six months after the receipt of the report.

Recommendation

The department should ensure that nonprofit subrecipients promptly submit the required audit reports and correct any deficiencies the audit reports identify. Furthermore, the department should promptly review the audit reports in order to ensure that the audit findings are resolved within six months after receipt of the report.

Item 5. Food Vouchers Issued to Unauthorized Vendors

Finding

The department cannot document that it adequately notifies local agencies who receive federal Special Supplemental Food Program for Women, Infants, and Children (WIC) monies of unauthorized vendors and that local agencies return any unauthorized vendor cards. For 11 of 13 unauthorized vendors tested, we found that the department could not provide us with evidence that it notified the appropriate local agencies that these vendors were no longer authorized to participate in the WIC program. As a result, the local agencies continued to issue food vouchers for these unauthorized vendors. For the remaining two unauthorized vendors, the department did have evidence it notified the local agencies. However, for one of these two vendors, the department notified the local agency of the agreement expiration in a letter dated November 2, 1989, yet the local agency continued to issue vouchers for this vendor through October 1992. If the department does not notify the local agencies that a vendor is no longer authorized to participate in the WIC program and ensure that the local agencies return unauthorized vendor cards, the local agencies may continue to issue food vouchers for unauthorized vendors.

According to the Chief of the Vendor Management Section, in January 1994, staff was assigned to reconcile the vendor cards assigned to the local agencies with the WIC system and to consult with local agencies to correct any errors. As a result of this reconciliation, the department is issuing new vendor cards or is requesting that the local agencies return vendor cards. Additionally, the department is now issuing letters advising the local agencies to return the vendor cards as unauthorized vendors are identified. The department has also implemented a new system for tracking the vendor cards.

Criteria

The Code of Federal Regulations, Title 7, Section 246.12(e) and (f), requires that only vendors authorized by the state agency may redeem food instruments and the state agency shall ensure that all participating food vendors have written contracts or agreements with the State. In addition, the WIC state plan states that the department will notify local agencies of the vendors deleted from the WIC program.

Recommendation

The department should ensure that it notifies local agencies of all unauthorized vendors and that local agencies return any unauthorized vendor cards.

**Item 6.
Lack of Site
Reviews**

Finding

The department did not conduct all required biennial site reviews for the administration of its WIC program. Specifically, the department did not conduct biennial site reviews during the two years ending September 30, 1993, for 26 of approximately 80 local agencies. In addition, the department had not finalized or issued a review letter as of November 15, 1993, for three of four site reviews completed during fiscal year 1992-93 that we chose to review. Without such site visits, which include reviews to determine whether the local agencies provide appropriate nutrition assessments, the department lacks assurance that the local agencies are complying with requirements of the WIC program. The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92.

Criteria

The Code of Federal Regulations, Title 7, Section 246.6(b), states that local agencies providing WIC services should meet specific requirements in dispensing services to beneficiaries. As part of the department's procedures to ensure that local agencies meet these requirements, the California State Plan for operation of the Special Supplemental Food Program for Women, Infants, and Children requires the department to conduct a biennial site review at each local agency. Additionally, the WIC program manual, Section 150-10, states that the review process will include an evaluation of nutrition assessment and that a review letter will be issued upon completion of the site review to notify the local agency of any areas of noncompliance. The program manual also states that the local agency then has 60 days to respond, detailing the corrective action taken or planned, as a result of the review.

Recommendation

The department should complete the required site reviews of local agencies.

**Item 7.
Food Vouchers
Not Reconciled
Promptly**

Finding

For the first eight months of fiscal year 1992-93, the department reconciled 99 percent of the food vouchers it issued with the food vouchers participants redeemed through the WIC program by the required timelines. The department is required to complete the reconciliation within 150 days of the first day of authorized use. However, the department was late in reconciling 34 percent of the food vouchers for March 1993 and 99 percent of the food vouchers for the

remaining three months of the fiscal year. Failure to promptly reconcile the vouchers may delay detection of irregularities such as redemption of fraudulent food vouchers.

The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness during its audits for fiscal years 1987-88 through 1990-91. According to the Chief of the WIC Supplemental Food Branch, the department is currently developing a new automated system that includes ensuring the timely reconciliation of food vouchers. As a result of the automation effort, the department expects the reconciliation process to require significantly less than 120 days. The department plans to implement the new system beginning July 1994, with 40 percent of the WIC caseload to be converted by October 1, 1994, and 100 percent by January 1996.

Criteria

The Code of Federal Regulations, Title 7, Section 246.12(n)(1), requires the department to reconcile the food vouchers it issued with the food vouchers redeemed by participants within 150 days of the first date of authorized use.

Recommendation

The department should continue its efforts to reconcile the food vouchers it issued with the food vouchers redeemed by participants within the required timelines.

Item 8. Suspension of Procedures for Detecting and Resolving Dual Enrollment

Finding

In July 1987, the department suspended its procedures for detecting dual enrollment in the WIC program because the procedures did not operate as intended and produced inaccurate reports. These reports were intended to detect WIC participants who may have enrolled at more than one location. The department's failure to produce accurate reports reduced its ability to detect and resolve participant abuses.

The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness during its audits for fiscal years 1987-88 through 1990-91. According to the Chief of the WIC Supplemental Food Branch, the new automated system described in Item 7 will include a mechanism for detecting dual participation and will be fully implemented by January 1996.

Criteria

The Code of Federal Regulations, Title 7, Section 246.7(k), requires the department to detect instances of dual participation.

Recommendation

The department should continue its efforts to establish reliable procedures to detect instances of dual participation.

Item 9. Improper Cash Management

Finding

The department maintained a balance of federal funds for the WIC program that exceeded the department's immediate cash needs. For example, in January 1993, the department requested approximately \$2.5 million more of federal funds than it needed to pay administrative costs. A combination of similar requests for funds resulted in the department returning to the federal government excess funds totaling approximately \$10.3 million for the fiscal year 1992-93 grant award. The department returned these funds by offsetting federal draws in the month of February 1994. This condition exists because the department did not prepare periodic reconciliations that compared actual expenditures with the federal funds received until the closeout of the grant in February 1994. After the department identified this as a problem, accounting staff began preparing a monthly reconciliation for its fiscal year 1993-94 grant award.

Criteria

The Code of Federal Regulations, Title 31, Section 205.4(a), requires that cash advances be as close as administratively feasible to the actual disbursement by the recipient organization.

Recommendation

The department should ensure that its requests for federal funds are limited to its immediate cash needs.

Item 10. Noncompliance With Certain Federal and State Requirements

Finding and Criteria

In the following instances, the department did not always comply with administrative requirements of the federal government:

- For 2 of 13 claims that we reviewed for the federal Maternal and Child Health Services Block Grant, the department held the related grant funds of \$139,120 and \$89,891 for 21 and 70 days, respectively, before disbursing to subrecipients. The Code of Federal Regulations, Title 31, Section 205.4(a), requires that cash

advances be as close as administratively feasible to the actual disbursement by the recipient organization. This section also stipulates that the timing and amount of cash advances be as close as administratively feasible to the actual disbursement by the recipient organization.

- The department's final request for advance or reimbursement report dated June 7, 1993, for the WIC program for the federal fiscal year ended September 30, 1992, did not reconcile to the accounting records. Specifically, the department reported approximately \$2,000 more in expenditures for food than it recorded in its accounting records. In total, the department reported approximately \$195 million in expenditures for food for this fiscal year. The Code of Federal Regulations, Title 7, Section 246.13(c), requires the department to maintain records that adequately identify the source and use of funds spent for program activities. Further, the State Administrative Manual, Section 20014, requires agencies receiving federal funds to reconcile federal financial reports with the official accounting records.
- The federal financial status reports for the Refugee and Entrant Assistance-State Administered programs for fiscal year 1992-93, did not reconcile with the official accounting records. Specifically, the department reported approximately \$2,000 less in expenditures than it recorded in its accounting records. In total, the department reported approximately \$27.9 million in expenditures for this federal program. The Code of Federal Regulations, Title 45, Section 74.73(a) and (b) requires the department to prepare financial status reports that indicate the amount of grant funds received and spent. The State Administrative Manual, Section 20014, requires agencies receiving federal funds to reconcile federal financial reports with the official accounting records.
- During the months of January through September 1993, the department's documentation of the physical inventory count of food vouchers for the WIC program indicates that the count was conducted by only one warehouse employee. The documentation contains no evidence that a second, independent person assisted in completing or verifying the inventory count. The Code of Federal Regulations, Title 7, Section 246.12(1), requires the department to ensure the secure storage of unissued food instruments. The WIC Program Manual, Section 3-49, requires that warehouse staff and an independent employee conduct an inventory of the vouchers in stock in the WIC warehouse.

- Of 40 automated Medi-Cal payments we tested, the department was not able to provide us with an assessment form for one payment totaling approximately \$70 made to a provider for the Child Health and Disability Prevention program. The assessment form acts as the invoice for this program. As a result, we were not able to determine the appropriateness of the payment nor whether the payment was federally reimbursed. The State Administrative Manual, Section 8422.1, requires state agencies to retain a copy of each invoice.

Although individually these deviations may appear to be insignificant, they do represent noncompliance with federal and state regulations which are designed to protect the public's resources from abuse.

Recommendation

The department should improve its compliance with federal and state requirements.

Department of Mental Health

We reviewed the Department of Mental Health's (department) administration of the U.S. Department of Health and Human Services grants, Federal Catalog Numbers 93.778 and 93.992.

Item 1. Cost Reports Not Always Obtained From Counties

Finding

During our review of the department's final allocation summary for fiscal year 1992-93, we determined that of the 54 counties participating in the Alcohol and Drug Abuse and Mental Health Services Block Grant (block grant), 10 failed to submit a final cost report to the department. The final cost report is an annual report of expenditures, due after the close of the reporting fiscal year. In addition, we determined that 4 of the 10 counties did not submit any quarterly cost reports during the fiscal year. We also determined that 2 of the 10 counties failed to submit at least one quarterly cost report during the fiscal year. Finally, we noted that one county that did submit a final cost report had not submitted any quarterly cost reports.

Late or unsubmitted reports limit the department's ability to monitor the expenditure of block grant funds. As a result, the department cannot ensure that block grant funds are being used for their intended purpose.

Criteria

The State Administrative Manual, Section 8760, requires all grant recipients of block grant funds to submit quarterly reports to the administering department within 20 days of the end of each quarter. In addition, the department's Final Allocation and Cost Report Policy for fiscal year 1992-93 states that counties must submit their final cost reports to the department by January 30, 1994.

Recommendation

The department should ensure that counties submit their quarterly and final cost reports by the required due dates.

Item 2. Failure To Adequately Monitor Cash Reports

Finding

The department does not adequately monitor the cash balances of subrecipients of the Alcohol and Drug Abuse and Mental Health Services block grant. During our review of quarterly reports that 10 counties submitted to the department, we noted that 4 of the counties had cash balances that exceeded expenditure levels by more than 15 percent. Furthermore, one of the 4 counties had a cash balance that exceeded its expenditure level by more than 140 percent. Finally, we determined that the department did not withhold or adjust subsequent monthly advances for any of these 4 counties.

The department advances 1/12th of the county's yearly allocation each month. To monitor cash on hand, the department receives quarterly cash reports; if cash on hand exceeds 15 percent of the county's expenditure level, future advances should be adjusted. However, the department does not appear to be following its own procedures. The department's procedures are designed to limit cash balances of subrecipients. By not following these procedures, the department does not ensure that it limits monthly cash advances to the minimum and immediate needs of the subrecipients. Consequently, the State may be advancing federal funds to subrecipients before they need the funds. If the department fails to limit cash advances to subrecipients' minimum and immediate needs, it could jeopardize future advances of block grant funds.

Criteria

The Code of Federal Regulations, Title 31, Section 205.4(a), requires that cash advances to a primary recipient be limited to the minimum amounts needed and be timed in accord with only the actual, immediate cash requirements of the recipient. In addition, Section 205.4(e) requires that advances by primary recipients to subrecipients conform substantially to those same standards of timing and amount. Finally, the California Government Code, Section 13401, requires agencies to ensure that a satisfactory system of internal controls is in place to provide effective accounting control over assets, liabilities, revenues, and expenditures.

Recommendation

The department should review quarterly cash reports to determine whether it needs to adjust cash advances to subrecipients so that cash on hand is limited to amounts required for immediate needs.

**Item 3.
Failure To
Comply With
the Drug-Free
Workplace Act**

Finding

The department is not complying with the Drug-Free Workplace Act (act). During our review, we interviewed 10 employees engaged in the performance of the block grant and determined that 6 had not received a copy of the department's drug-free workplace policy. Furthermore, we determined that 3 of the 6 employees are supervisors. Failure to comply with the act could jeopardize future receipt of block grant funds.

Criteria

The Drug-Free Workplace Act of 1988 requires grantees to publish a policy notifying employees that the unlawful manufacture, distribution, dispensing, possession, or use of a controlled substance is prohibited in the grantee's workplace, and specifying the actions that will be taken against the employees for violation of such prohibition. In addition, the act requires grantees to give each employee engaged in the performance of the grant a copy of the policy.

Recommendation

The department should ensure that each employee engaged in the performance of the block grant receives a copy of the department's drug-free workplace policy.

Department of Social Services

We reviewed the financial operations and related internal controls of the Department of Social Services (department) and the department's administration of the U.S. Department of Agriculture grants, Federal Catalog Numbers 10.551 and 10.561; the U.S. Federal Emergency Management Agency grant, Federal Catalog Number 83.516; and the U.S. Department of Health and Human Services grants, Federal Catalog Numbers 93.560 (formerly 93.020), 93.561 (formerly 93.021), 93.563 (formerly 93.023), 93.566 (formerly 93.026), 93.645, 93.658, 93.659, 93.667, and 93.802.

Item 1. Inaccurate Reporting of Time Charges for the Social Security Disability Insurance Program

Finding

The department did not accurately report to the federal government the time charged by department personnel for the Social Security Disability Insurance program. Specifically, during our review of the quarter ended March 31, 1993, we noted the following:

- The department understated the employee time charges for the Social Security Disability program reported on the quarterly federal report by approximately 1,200 hours.
- For 3 of the 16 employee time reports that we reviewed, the department did not include eleven hours of employee leave on the attendance report that was identified on the related employee absence report. Additionally, for another employee, the department was unable to provide support for 36 hours of leave reported on the attendance report.

Criteria

The Code of Federal Regulations, Title 20, Section 404.1625, requires the department to maintain the records and reports relating to the administration of the disability programs. In addition, the State Administrative Manual, Section 8539, requires that state agencies maintain complete records of attendance and absences for each employee during each pay period.

Recommendation

The department should ensure that adequate support is maintained for reporting time charges and that time charges are accurately reported on the quarterly federal financial reports.

Item 2. Federal Financial Reports Not Reconciled with Accounting Records

Finding

The department did not reconcile its federal financial reports prepared during fiscal year 1992-93 with the departmental accounting records. Failure to reconcile federal financial reports with the accounting records can result in misstatements of claims that may go undetected.

The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness during its audits for fiscal years 1985-86 through 1990-91. In its response, the department stated that it is in the process of developing an automated process designed to ensure that the data contained in federal reports are consistent with the accounting records maintained in the California State Accounting and Reporting System. Although the department estimated that the process would be completed by July 1, 1993, the process has not been completed as of April 1994.

Criteria

The Office of Management and Budget, Circular A-102 Revised, Subpart C, paragraph 883(b)(1), requires that grantees provide accurate, current, and complete disclosure of each grant program. Further, the State Administrative Manual, Section 20014, requires agencies receiving federal funds to reconcile federal financial reports with the official accounting records and retain all supporting schedules and worksheets for a minimum of three years.

Recommendation

The department should implement a reconciliation system so that it can reconcile its federal financial reports with departmental accounting records.

Item 3. Noncompliance With Additional Federal Requirements

Finding

We noted the following instances when the department did not always comply with the requirements of the federal government.

- The department understated the federal and state shares of expenditures by approximately \$4,000 for the Job Opportunities and Basic Skills (JOBS) Training program for the quarter ended March 31, 1993. Specifically, the department did not report expenditures that exceeded the allowable limit for expenditures funded by the federal government at a 90 percent rate. Further, the department should have reported these costs as expenditures funded by the federal government at a 50 and 60 percent rate since they

were legitimately covered by those funding rates. The Code of Federal Regulations, Section 250.73(b), states that the federal government's share of JOBS expenditures will be 60 percent and 50 percent for certain support costs.

- The department overstated the cash on hand balance for the federal Family Support Payments to States-Assistance Payments program for the quarter ending June 30, 1993, by approximately \$7,100. The Code of Federal Regulations, Title 45, Section 74.61(a), requires that accurate, current, and complete disclosure of the financial results of each project or program shall be made in accordance with the financial reporting requirements of the grant.
- The department does not always ensure that counties properly review and maintain timesheets that are used as a basis for payment for In-Home Support Services (IHSS) providers. Specifically, 3 of the 20 provider timesheets we tested did not total to the correct number of hours. According to an IHSS policy analyst, although individuals may have been paid for more hours than the total of their reported daily hours worked, the electronic data processing system that processes these payments has an edit which ensures that individuals are not paid more than the total hours of service authorized for the IHSS recipient. Additionally, three of the 20 provider timesheets that we requested from the counties could not be located. The Office of Management and Budget, Circular A-102 Revised, Subpart C, paragraph 883A(b)(6), requires that the department and counties maintain accounting records that are supported by source documents.
- The department completed only seven pages of the ten-page quarterly statement of expenditures for the Foster Care—Title IV-E program. Revised federal reporting instructions from the Administration for Children, Youth, and Families indicate the information to be included on the quarterly statements of expenditures. Since June 30, 1990, the department has been required to submit a ten-page quarterly statement of expenditures. Previously, the department was only required to submit a two-page report. The federal Department of Health and Human Services estimated that the revised statement could be completed in approximately 25 hours. However, in a letter submitted to the federal government on May 14, 1990, the department stated that the new report would require extensive system modifications and a significant increase in staff time. As a result, the department would not be able to provide all the information required for the new report.

Although individually these deviations may appear to be insignificant, they do represent noncompliance with federal regulations which are designed to protect the public's resources from abuse.

Recommendation

The department should improve its compliance with federal requirements.

Legislative, Judicial and Executive

Office of Emergency Services

We reviewed the Office of Emergency Services' (office) administration of the U.S. Federal Emergency Management Agency grant, Federal Catalog Number 83.516.

Delay in Appealing Denied Costs

Finding

The office has not appealed the Federal Emergency Management Agency's (FEMA) denial of approximately \$7.7 million of claimed expenses related to the Loma Prieta earthquake. The Bureau of State Audits reported a similar weakness during our audit for fiscal year 1991-92 and the Office of the Auditor General reported a similar weakness during its audit for fiscal year 1990-91. As of October 26, 1993, the office had not appealed this determination although the office previously indicated that it planned to make its appeal by May 29, 1992.

Criteria

Section 0911.4 of the State Administrative Manual requires state agencies to secure prompt reimbursement from grant funds for goods and services provided. Consequently, if it believes the FEMA erred in its denial of approximately \$7.7 million of claimed expenses related to the Loma Prieta earthquake, the office should promptly appeal the FEMA's denial of its claims. The Code of Federal Regulations, Title 44, Section 206.206, describes the process for appealing denied costs.

Recommendation

The office should appeal \$7.7 million in claims denied by FEMA during fiscal year 1990-91.

Item 2. Failure To Promptly Collect All Overpayments From Applicants

Finding

During fiscal year 1992-93, the office did not promptly collect \$183,350 in overpayments made to five applicants (recipients of disaster assistance funds are referred to as "applicants") for disaster grants. Additional records at the office indicate that other applicants owe the office more than \$900,000 in overpayments. Some of these debts date back to 1987. Because the office did not promptly collect the \$183,350 in overpayments, the FEMA withheld \$183,350 from a disaster grant awarded to the State Department of Parks and Recreation. (According to the chief deputy director, the office subsequently used funds from the National Disaster Assistance Account to reimburse the

State Department of Parks and Recreation to ensure it received its full grant amount.) The office has billed the delinquent applicants, but it has not collected the \$183,350 from the five applicants because, according to the office's chief deputy director, the office has not adopted procedures for following up on applicants that do not pay. However, the office informed us that they are developing these procedures.

Criteria

The Code of Federal Regulations, Title 44, Section 205.120(c), states that bills for collection are due upon receipt. We interpret this to mean that the office, barring appeals from the applicants, should collect the overpayments within 30 days of a bill for collection and should return the overpayments to the FEMA within 60 days of a bill for collection. If the office does not remit the funds to the FEMA within 60 days, the FEMA can withhold funds from a future disaster grant to collect the overpayment from the office.

Recommendation

The office should promptly collect overpayments from applicants. Furthermore, the office should adopt procedures for promptly collecting overpayments from applicants.

Item 3. Delay Between Receipt and Return of Federal Funds

Finding

The office did not always promptly remit to the FEMA refunds of federal funds that applicants have not used. The FEMA bills applicants for amounts they are to refund to the FEMA. Applicants send the refunds to the office, and the office remits the refunds to the FEMA. For 2 of the 6 refunds that we reviewed, the office took 36 and 134 days to remit the funds to FEMA. We observed a similar weakness during our audits of the office for fiscal years 1988-89, 1989-90, and 1990-91.

Criteria

The Code of Federal Regulations, Title 44, Section 205.120(c), states that bills for collection are due upon receipt. We interpret this to mean that the State should return to the FEMA amounts refunded by disaster applicants within 30 days.

Recommendation

The office should promptly remit refunds from applicants to the FEMA.

State and Consumer Services Agency

California Museum of Science and Industry

We reviewed the California Museum of Science and Industry's (museum) internal controls and accounting procedures for cash collected from special event parking and from parking meters along Exposition Boulevard.

Item 1. Inadequate Controls Over Parking Receipts From Special Events

Finding

The museum's accounting controls and procedures for the cash receipts from special event parking are inadequate. Specifically, there is a lack of separation of duties among museum personnel who handle cash receipts from special event parking. The parking supervisor controls the sequentially numbered parking tickets before, during, and after the special event. The parking supervisor also collects the cash for special event parking. After the event is over, the supervisor counts the cash from special event parking. The supervisor also accounts for the sequentially numbered parking tickets. Since the parking supervisor accounts for both the cash collected and the number of tickets sold, there is no independent reconciliation of cash collected to the number of tickets sold. In fiscal year 1992-93, the museum collected approximately \$48,000 from special event parking. Failure to maintain proper separation of duties can result in errors, irregularities, or illegal acts that may go undetected for extended periods of time.

Also, the supervisor accounts for cash overages and shortages from special event parking. The parking supervisor maintains a cash fund in the parking office safe for cash overages and shortages. Cash overages or shortages occur when the number of parking tickets sold multiplied by the parking price does not reconcile with the cash collected. For example, if a cash overage occurs, the supervisor maintains the cash overage in the parking office safe until a shortage occurs. Then, the supervisor uses the cash overage to correct for the cash shortage.

Further, the parking supervisor maintains control of cash collected from the special event parking day, generally Saturdays or Sundays, until the next business day, generally Mondays. After the supervisor counts the cash, he places it in the parking office safe until the next business day. The safe is located in a small room without windows in the parking office. The parking supervisor also controls access to the safe. However, since there is no independent reconciliation of the parking receipts and one person controls access to the parking office safe, irregularities may occur after the funds are placed in the safe.

Moreover, there are no signs in the parking areas notifying the public that parking personnel must provide a parking ticket when a customer purchases a ticket. Further, there are no signs providing the public with a telephone number to call if the customer does not receive a parking ticket in exchange for cash. Also, the parking tickets do not state that they must be visible in the vehicle (that is, placing the ticket on the car's dashboard or under the windshield wiper).

Criteria

Good accounting procedures require that all cash receipts be deposited and not held for future uses. Also, the State Administrative Manual, Section 8071, requires that cash overages be recognized in the accounting records at the time of receipt. Further, the manual requires that cash shortages be written off and that a report be submitted to the Department of Finance describing the causes of the shortage. In addition, the museum's practice of maintaining this cash fund in the parking office increases the risk of loss from theft or fire. Finally, the California Government Code, Sections 13402 and 13403, requires state offices to ensure that a satisfactory system of internal and administrative controls is in place to provide effective controls over assets, liabilities, revenues, and expenditures.

Recommendation

The museum should correct the control weaknesses described above to ensure that parking receipts from special events are adequately safeguarded.

Item 2. Inadequate Controls Over Parking Receipts From Meters

Finding

The museum had inadequate accounting controls and procedures for the cash collected from parking meters along Exposition Boulevard. In fiscal year 1992-93, the museum collected approximately \$45,000 from these meters. A lack of separation of duties among museum personnel exists. The parking personnel who collect the cash from the parking meters have access to the locked cash collection box.

After a parking meter is opened, the parking personnel, including the parking supervisor, remove a locked cylinder from the parking meter. They then place the locked cylinder into the collection box and turn the cylinder. The turning of the cylinder in the collection box unlocks the cylinder and causes the coins to drop into the collection box. The cylinders are designed to prevent the parking personnel from accessing the cash. At the end of the collection process, the parking supervisor unlocks the collection box. Then, the parking personnel

remove the coins from the collection box and place the coins collected into a cash bag. During this process, a public safety officer is present. In addition, if accounting personnel are available, the accounting personnel open the countroom and the safe and then place the cash bag into the safe. However, if accounting personnel are not available, the parking supervisor places the cash bag into the safe in the parking office. But, as stated before, the parking supervisor has access to the safe.

Criteria

Good accounting practices require that the personnel who collect the cash should not have access to the cash collection box. Instead, the cash collection box should be placed unopened into the countroom safe or the parking office safe. Failure to maintain proper separation of duties can result in irregularities or illegal acts that may go undetected for extended periods of time. In addition, the California Government Code, Sections 13402 and 13403, requires state offices to ensure that a satisfactory system of internal and administrative controls is in place to provide effective controls over assets, liabilities, revenues, and expenditures.

Recommendation

The museum should correct the control weaknesses described above to ensure that receipts from parking meters are adequately safeguarded.

Department of General Services

We reviewed the financial operations and related internal controls of the Department of General Services (department).

Possible Liability to the Federal Government

Item 1. Finding

The department has a possible liability to the federal government estimated to be as much as \$7.1 million for profits it has accumulated in its Service Revolving Fund (SRF) between July 1, 1984, and June 30, 1993. The department's SRF is an internal service fund that accounts for printing and procurement services to state agencies. The department has charged these agencies more than its costs for providing services. In turn, state agencies have passed these charges on to federal programs. The SRF accumulates profits when the department's charges for services exceed its costs. Federal regulations prohibit the State from charging federal programs for more than its costs.

In 1984, the federal Department of Health and Human Services (DHHS) audited the State's rate-setting methods for internal service funds. As a result of the audit, the State was required to refund to the federal government approximately \$14.9 million of the profits accumulated in internal service funds. This amount represented the federal share of profits accumulated in five of the State's internal service funds from July 1, 1969, to June 30, 1984. The Department of Finance agreed that 15.5 percent of the SRF's accumulated profits of approximately \$66.8 million at June 30, 1984, resulted from charges to federal programs and, thus, the SRF owed the federal government approximately \$10.3 million.

The DHHS is conducting an audit of the State's rate-setting methods for internal service funds for the period July 1, 1984, through June 30, 1991. However, as of April 30, 1994, the DHHS has not issued its final audit report. Thus, using procedures similar to those of the Department of Finance, and using the same ratio of 15.5 percent developed as a result of the 1984 audit, we estimate that, under current federal regulations, the State may owe the federal government approximately \$7.1 million.

However, an October 1988 proposed amendment to the federal Office of Management and Budget (OMB), Circular A-87, would allow state agencies a reasonable working capital reserve of 60 days' worth of cash

expenditures. Although the revisions to OMB Circular A-87 have not been finalized, in 1991, the DHHS authorized the State of Oregon to retain sufficient funds to cover up to 60 days' working capital. In January 1994, the State requested a similar authorization. However, according to correspondence dated May 6, 1994, the DHHS will not respond to the State's request until the current federal audit is complete. If the State is allowed to retain a 60-day working reserve, its liability to the federal government may be eliminated.

If the department has a liability, it may not be able to reimburse the federal government because then the SRF's fund balance may be reduced to the point at which it does not have sufficient working capital to operate. At the end of the fiscal year 1992-93, the department's working capital for the SRF was approximately \$17.3 million. This amount is only enough to cover approximately 17.4 days of the department's cash expenditures in the SRF.

The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar finding during its audits for the fiscal years 1988-89 through 1990-91. The state auditor and the auditor general recommended that the Department of Finance ensure state agencies comply with federal regulations. In his response of December 24, 1993, the director of the Department of Finance stated that the State's internal service funds meet the State's laws and regulations. However, in some cases, state laws and regulations differ from those of the federal government. The director further stated that when the amendments to OMB Circular A-87 are approved, the State would review the guidelines for its internal service funds.

Criteria

OMB Circular A-87, "Cost Principles for State and Local Governments," does not allow the State to charge federal programs for amounts that exceed costs. In addition, the California Government Code, Section 13070, provides the Department of Finance with general powers of supervision over all matters concerning the financial and business policies of the State.

Recommendation

The department should comply with OMB Circular A-87 when establishing billing rates for charges to state agencies receiving federal support. Further, the Department of Finance should ensure that the department complies with federal regulations. For example, compliance could be ensured by developing guidelines for the

department and state agencies receiving services from the department. In addition, the Department of Finance should continue to monitor the proposed amendment to OMB Circular A-87 to determine its effect on state charges to federal programs.

**Item 2.
Completed School
Construction
Projects Not
Audited Promptly**

Finding

The department's Office of Local Assistance (OLA) did not complete close-out audits of school construction projects promptly. According to data provided by the OLA, as of March 1994, approximately 1,200 school construction projects were ready for close-out audits. Of these, 204 have been ready for close-out audits for more than four years. Because it has not reviewed these projects, the OLA has not yet determined the amount of the districts' allowable expenditures and has not determined whether the State owes districts additional funds or whether any funds that may have been apportioned to these projects in excess of actual costs are to be returned to the State and made available for other projects. According to data provided by the OLA, 294 close-out audits were completed between January 1992 and March 1994. These audits disclosed that certain school districts owed the State approximately \$2.9 million and the State owed other school districts approximately \$11.8 million of the districts' remaining apportioned amounts.

The Bureau of State Audits reported a similar weakness during the audit for fiscal year 1991-92, and the Office of the Auditor General reported a similar weakness in a January 1991 report entitled "Some School Construction Funds Are Improperly Used and Not Maximized." In its response to our fiscal year 1991-92 management letter, the department stated that the Department of Finance has approved additional audit positions. The department estimates that, with the additional auditors, the backlog of close-out audits will be eliminated within two years.

Criteria

The California Government Code, Section 13401, requires agencies to maintain an effective system of internal control. Section 13403 requires that the system of internal control include recordkeeping procedures sufficient to provide effective control over assets, liabilities, revenues, and expenditures. Furthermore, the State Administrative Manual, Section 8776.6, requires each department to develop procedures that will ensure prompt follow-up on receivables. Prompt

close-out audits would enable the department to determine whether the school districts owe the State money for amounts distributed in excess of actual construction costs.

Recommendation

The OLA should ensure the prompt audit of closed construction projects.

Item 3. Inadequate Control Over Accounting Records

Finding

The department's Office of Local Assistance (OLA) maintained inadequate controls over its accounting records for the State School Building Lease-Purchase Fund (fund 344); the School Facilities November 1988 Bond Account, State School Building Lease-Purchase Fund (fund 776); and the School Facilities June 1988 Bond Account, State School Building Lease-Purchase Fund (fund 789). Specifically, for 21 of the 185 projects we reviewed, the OLA's subsidiary project records, which document the detailed funding history of each project, differed from the amounts reflected on the budget report for the projects. The budget report supports the general ledger. In 17 instances, the budget report was in error, and in 2 instances, the project records were in error. In addition, for 2 of the 21 projects, both the project records and the budget report were in error. As of June 30, 1993, the project records for 19 of the 21 projects still differed from the amount reflected on the budget report for the project. When project records were in error, the OLA did not have accurate information readily available about the remaining funds for projects before distributing funds to school districts. When the budget report was in error, the account balances reported to the State Controller's Office as of June 30, 1993, were incorrect. For example, the account balances for due to local governments in funds 776 and 789 were understated by approximately \$1.0 million and \$1.6 million, respectively. The balance for due to local governments in fund 344 was overstated by approximately \$1.1 million.

The Bureau of State Audits reported similar weaknesses during the financial audit for fiscal year 1991-92, and the Office of the Auditor General reported similar weaknesses during the financial audits for fiscal years 1987-88 through 1990-91.

Criteria

The California Government Code, Section 13401, requires agencies to maintain an effective system of internal control. In addition, the Government Code, Section 13403, requires that the system of internal

control include recordkeeping procedures sufficient to provide effective accounting control over assets, liabilities, revenues, and expenditures. Furthermore, the State Administrative Manual, Section 7800, requires subsidiary ledgers to be reconciled with the general ledger each month, and the State Administrative Manual, Section 7900, discusses the importance of making regular reconciliations. Properly prepared reconciliations represent an important element of internal control because they provide a high level of confidence that the financial records are complete.

Recommendation

The OLA should reconcile its subsidiary project records with its general ledger each month and promptly correct any errors.

Item 4. Inaccurate Analysis of Liabilities in the Architecture Revolving Fund

Finding

The department did not adequately analyze and report its year-end liabilities in the Architecture Revolving Fund (ARF). Specifically, the department included in its accounts payable accrual amounts for claims filed between July 1 and July 31, 1993. However, approximately \$1.7 million of the amount accrued related to services received after June 30 and, therefore, should not have been reported as a liability. The department also overstated its liability for open purchase and service orders by approximately \$309,000. Of this amount, approximately \$195,000 was for goods and services that had not been received by June 30, 1993. The remaining \$114,000 was for invoices that had been paid or were canceled before June 30, 1993. Because the department did not adequately analyze its year-end liabilities, accounts payable and expenditures in the ARF were overstated by approximately \$2 million.

Criteria

The State Administrative Manual, Section 10544, requires state agencies to review their records to ensure that they have accurately recorded all amounts owed to others at June 30.

Recommendation

The department should analyze its year-end liabilities and review supporting documents to ensure that it only accrues amounts for goods and services received but not paid for as of June 30.

Item 5. Noncompliance With State Requirements for the Architecture Revolving Fund

Finding and Criteria

In the following instances, the department did not always comply with state requirements related to the Architecture Revolving Fund (ARF):

- The department did not always return unencumbered funds to depositing agencies within three months after completion of the projects, as required by California Government Code, Section 14959. Specifically, for 16 of the 20 projects we reviewed, the department took from just over 3 months to 55 months to return the unencumbered funds totaling approximately \$499,000. In 12 of the instances, the department requested the return of funds from the ARF within the required 3 months. However, the Department of Finance and the State Controller's Office took up to 7 months to process these requests totaling approximately \$443,000.
- The department did not always return unencumbered funds within three years from the time the funds were originally transferred to the ARF, as required by the California Government Code, Section 14959. Specifically, the department did not return approximately \$149,000 promptly for 4 of the 20 projects we reviewed for which funds were transferred to the ARF before June 30, 1990.
- The department did not always bill for services promptly. In November 1993, we reviewed 10 construction projects that had a receivable balance at June 30, 1993. For 7 of the 10 construction projects, the department failed to bill promptly or had not yet billed for receivables totaling approximately \$378,000. The State Administrative Manual, Section 8776.3, requires that agencies prepare and send an invoice as soon as possible after recognition of a claim.

The Bureau of State Audits reported similar weaknesses during its audit for fiscal year 1991-92.

Recommendation

The department should ensure that it returns unencumbered funds promptly. In addition, the department should promptly bill for amounts receivable.

**Item 6.
Noncompliance
With State
Requirements**

Finding and Criteria

In the following instances, the department did not always comply with administrative requirements of the State:

- The department is not conducting the required audits of agencies granted purchase delegation authority. Specifically, as of August 1993, the department had delegated purchasing authority to 151 agencies. However, the department had not audited 80 of the agencies within three years, as required by the California Public Contract Code, Section 10333(5)(b).
- The department's Office of State Printing modified a purchase order, substituting additional training for an item of equipment, valued at \$2,500, without obtaining the approval of the department's Office of Procurement. The State Administrative Manual, Section 3566, requires purchase order changes or revisions to be prepared by the Office of Procurement. Section 3566.1 requires purchase order changes when there is a change in description specifications or substitution of any material.

Recommendation

The department should improve its compliance with each of the state requirements.

Youth and Adult Correctional

Department of the Youth Authority

We reviewed the Department of the Youth Authority's (department) administration of the U.S. Department of Agriculture grants, Federal Catalog Numbers 10.553 and 10.555.

Item 1. Inadequate Documentation of Wards' Eligibility

Finding

For those wards participating in the School Breakfast Program and National School Lunch Program (NSB/SL), the department did not always provide complete documentation of wards' birthdates. As a result, it was not clear whether or not the wards were under 21 years of age and therefore eligible for federal reimbursement from the NSB/SL programs.

Criteria

The Code of Federal Regulations, Title 7, Subchapter A, Sections 220.2(c) and 210.2(b), defines the eligibility for participation in the NSB/SL programs as being those persons enrolled in an institution participating in a school program and being under 21 years of age.

Recommendation

The department should ensure that adequate documentation of each ward's eligibility for participation in the NSB/SL programs is provided when claiming federal reimbursement. Adequate documentation includes the ward's full name, California Youth Authority identification number and birthdate.

Item 2. Incorrect Claim for Meals Not Served

Finding

We reviewed all of the department's monthly claims for fiscal year 1992-93. For three schools, we tested the supporting detail of the monthly claims. At one of the three schools, where we reviewed the supporting detail, we found that the supporting detail contained errors. In that supporting detail, the department made a clerical error that resulted in the department claiming approximately \$13,000 in reimbursements for 4,687 breakfasts and 4,612 lunches that were not served.

Criteria

The Code of Federal Regulations, Title 7, Subpart B, Sections 220.11(b) and 210.7(c), provides that to be entitled to reimbursement for meals under the NSB/SL programs, claims are limited to the number of meals served.

Recommendation

We recommend that the department ensure that it claims reimbursement only for meals served.

Report on Compliance With Federal Grant Requirements



CALIFORNIA STATE AUDITOR

BUREAU OF STATE AUDITS

KURT R. SJOBERG
State Auditor

MARIANNE P. EVASHENK
Chief Deputy State Auditor

Independent Auditors' Report on Compliance With Federal Grant Requirements

The Governor and Legislature of
the State of California

We have audited the general purpose financial statements of the State of California as of and for the year ended June 30, 1993, and have issued our report thereon dated April 30, 1994. The scope of our audit did not extend to financial aid programs administered by the California State University or to programs administered by the University of California because the California State University and the University of California contract with other independent certified public accountants for Office of Management and Budget (OMB) Circular A-133 audits. In addition, our audit of charges made by subrecipients of federal funds was limited to a review of the State's system for monitoring those subrecipients because subrecipients have OMB Circular A-128 audits or OMB Circular A-133 audits performed by other independent auditors.

The following sections provide our opinion on major federal programs, our report on general requirements for major federal programs, and our report on nonmajor federal programs.

Major Programs

We have also audited the State of California's compliance with the requirements governing types of services allowed or not allowed; eligibility; matching, level of effort, or earmarking of funds; reporting; special tests and provisions; federal financial reports and claims for advances and reimbursements; and amounts claimed or used for matching that are applicable to each of its major federal financial assistance programs. The major federal financial assistance programs for the year ended June 30, 1993, are identified in the schedule of federal assistance beginning on page 175. The State's management is responsible for the State's compliance with these requirements. Our responsibility is to express an opinion on compliance with these requirements based on our audit.

We conducted our audit of compliance with these requirements in accordance with generally accepted auditing standards, *Government Auditing Standards*, issued by the Comptroller General of the United States, and OMB Circular A-128, *Audits of State and Local Governments*. Those standards and OMB Circular A-128 require that we plan and perform the audit to obtain reasonable assurance about whether material noncompliance

with the requirements referred to above occurred. An audit includes examining, on a test basis, evidence about the State of California's compliance with those requirements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the State of California complied, in all material respects, with the requirements governing types of services allowed or unallowed; eligibility; matching, level of effort, or earmarking of funds; reporting; special tests and provisions that are applicable; federal financial reports and claims for advances and reimbursements; and amounts claimed or used for matching that are applicable to each of its major federal financial assistance programs for the year ended June 30, 1993.

Further, we have applied procedures to test the State of California's compliance with the following general requirements applicable to each of its major federal financial assistance programs, which are identified in the schedule of federal assistance beginning on page 175, for the year ended June 30, 1993: political activity, Davis-Bacon Act, civil rights, cash management, relocation assistance and real property acquisition, federal financial reports, allowable cost/cost principles, Drug-Free Workplace Act, and administrative requirements. Our procedures for testing compliance with these requirements were limited to the applicable procedures described in the OMB's *Compliance Supplement for Single Audits of State and Local Governments*. Our procedures were substantially less in scope than an audit, the objective of which is the expression of an opinion on the State of California's compliance with the requirements listed in the preceding paragraph. Accordingly, we do not express such an opinion on the general requirements.

Nonmajor Programs

In connection with our audit of the State of California's general purpose financial statements and with our consideration of the State's control structure used to administer federal financial assistance programs, as required by OMB Circular A-128, we selected certain transactions applicable to certain nonmajor federal financial assistance programs for the year ended June 30, 1993. As required by Circular A-128, we have performed auditing procedures to test compliance with the requirements governing types of services allowed, eligibility, and special tests and provisions that are applicable to those transactions. Our procedures were substantially less in scope than an audit, the objective of which is the expression of an opinion on the State's compliance with these requirements. Accordingly, we do not express such an opinion on the nonmajor programs.

With respect to all the items tested, the results of the procedures described above disclosed no material instances of noncompliance with the requirements identified in the preceding paragraphs. With respect to the items not tested, nothing came to our attention that caused us to believe that the State of California had not complied, in all material respects, with those requirements. However, the results of our audit procedures disclosed immaterial instances of noncompliance with those requirements. We discuss those instances of noncompliance and

present recommendations to correct them in the section of our report beginning on page 39. The instances of noncompliance identified in the State's single audit report for fiscal year 1991-92 that have not been corrected are also included in that section. Additionally, beginning on page 207, we present a schedule listing instances of noncompliance that we consider to be minor. We considered these instances of noncompliance in forming our opinion on compliance with requirements for major federal programs, which is expressed above.

This report is intended for the information of the Governor and Legislature of the State of California and the management of the executive branch. However, this report is a matter of public record, and its distribution is not limited.

BUREAU OF STATE AUDITS



SALLY L. FILLIMAN, CPA
Deputy State Auditor

April 30, 1994

**Report on the
Schedule of Federal Assistance**



CALIFORNIA STATE AUDITOR

BUREAU OF STATE AUDITS

KURT R. SJOBERG
State Auditor

MARIANNE P. EVASHENK
Chief Deputy State Auditor

Independent Auditors' Report on the Schedule of Federal Assistance

The Governor and Legislature of
the State of California

We have audited the general purpose financial statements of the State of California as of and for the year ended June 30, 1993, and have issued our report thereon dated April 30, 1994. These general purpose financial statements are the responsibility of management of the State of California. Our responsibility is to express an opinion on these general purpose financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the general purpose financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the general purpose financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Our audit was made for the purpose of forming an opinion on the general purpose financial statements of the State of California, taken as a whole. The accompanying schedule of federal assistance is presented for purposes of additional analysis and is not a required part of the general purpose financial statements. The Office of Management and Budget, Circular A-128, *Audits of State and Local Governments*, and the Single Audit Act of 1984 require the schedule of federal assistance to present total expenditures for each federal assistance program. However, although the state accounting system separately identifies revenues for each federal assistance program, it does not separately identify expenditures for each program. As a result, we present the schedule of federal assistance on a revenue basis. The schedule shows the amount of federal funds and the estimated value of food stamps and commodities received by the State for the year ended June 30, 1993. The information in that schedule has been subjected to the auditing procedures applied in the audit of the general purpose financial statements and, in our opinion, is fairly presented in all material respects in relation to the general purpose financial statements taken as a whole. The schedule does not include federal revenue received by the University of California or federal revenue for financial aid received by the California State University. These revenues

are audited by other independent auditors in accordance with the Office of Management and Budget, Circular A-133, *Audits of Institutions of Higher Education and Other Nonprofit Organizations*.

This report is intended for the information of the Governor and Legislature of the State of California and the management of the executive branch. However, this report is a matter of public record, and its distribution is not limited.

BUREAU OF STATE AUDITS



SALLY L. FILLIMAN, CPA
Deputy State Auditor

April 30, 1994

**Schedule of Federal Assistance for the
Fiscal Year Ended June 30, 1993**

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Department of Agriculture:		
Agricultural Conservation Program	10.063	\$ 26,000
Forestry Incentives Program	10.064	13,000
Farm Labor Housing Loans and Grants	10.405	2,942,000
Food Distribution	10.550	79,043,547 A *
Food Stamps	10.551	2,077,344,568 A *
School Breakfast Program	10.553	116,626,930 A
National School Lunch Program	10.555	510,025,269 A
Special Milk Program for Children	10.556	941,070
Special Supplemental Food Program for Women, Infants, and Children	10.557	311,582,767 A
Child and Adult Care Food Program	10.558	134,123,427 A *
Summer Food Service Program for Children	10.559	100,165 **
State Administrative Expenses for Child Nutrition	10.560	9,750,349
State Administrative Matching Grants for Food Stamp Program	10.561	218,866,238 A
Nutrition Education and Training Program	10.564	776,107
Commodity Supplemental Food Program	10.565	4,488,917 **
Temporary Emergency Food Assistance (Administrative Costs)	10.568	5,499,668

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Food Commodities for Soup Kitchens	10.571	3,517,212 **
Forestry Research	10.652	57,319
Cooperative Forestry Assistance	10.664	1,187,980
Schools and Roads—Grants to States	10.665	59,580,922 A
Other—Department of Agriculture	10.999	2,995,473
 Department of Commerce:		
Trade Development	11.110	125,056
Economic Development—Support for Planning Organizations	11.302	114,000
Special Economic Development and Adjustment Assistance Program— Sudden and Severe Economic Dislocation and Long-Term Economic Deterioration	11.307	152,342
Special Economic Development and Adjustment Assistance Program— Sudden and Severe Economic Dislocation	11.311	11,950
Anadromous Fish Conservation Act Program	11.405	274,982
Interjurisdictional Fisheries Act of 1986	11.407	187,066
Coastal Zone Management Administration Awards	11.419	2,314,575
Coastal Zone Management Estuarine Research Reserves	11.420	91,145

Footnotes are presented on page 198.

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Manufacturing Extension Program	11.611	485,392
Other—Department of Commerce	11.999	234,604
Department of Defense:		
Flood Control Projects	12.106	13,651
Navigation Projects	12.107	185,332
Planning Assistance to States	12.110	691,083
State Memorandum of Agreement Program for the Reimbursement of Technical Services	12.113	7,811,007
Selected Reserve Educational Assistance Program	12.609	319
Other—Department of Defense	12.999	1,773,487
Department of Housing and Urban Development:		
Community Development Block Grants/ Small Cities Program	14.219	156,871
Community Development Block Grants/ State's Program	14.228	22,828,153 A
Rental Housing Rehabilitation	14.230	52,198
Emergency Shelter Grants Program	14.231	2,910,202
Supportive Housing Program	14.235	770,290
Supplemental Assistance for Facilities to Assist the Homeless	14.236	124,188
Equal Opportunity in Housing	14.400	136,350

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Section 8 Rental Voucher Program	14.855	1,424,709
Lower Income Housing Assistance Program—Section 8 Moderate Rehabilitation	14.856	4,255,603
Section 8 Rental Certificate Program	14.857	17,757,383
Department of the Interior:		
Small Reclamation Projects	15.503	203,398
Fishery Research—Information	15.604	668,975
Sport Fish Restoration	15.605	10,818,474
Wildlife Restoration	15.611	5,875,444
Endangered Species Conservation	15.612	525,323
Geological Survey—Research and Data Acquisition	15.808	93,367
Historic Preservation Fund Grants-In-Aid	15.904	737,345
Outdoor Recreation—Acquisition, Development and Planning	15.916	2,033,633
Shared Revenue—Potash/Sodium Lease	15.999	23,145,152 A
Other—Department of the Interior	15.999	4,069,533
Department of Justice:		
Juvenile Justice and Delinquency Prevention—Allocation to States	16.540	5,102,359
Criminal Justice Statistics Development	16.550	146,061

Footnotes are presented on page 198.

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Justice Research, Development and Evaluation Project Grants	16.560	187,956
Mariel-Cubans	16.572	179,814
Criminal Justice Discretionary Grant Program	16.574	4,780,798
Crime Victim Assistance	16.575	6,279,033
Crime Victim Compensation	16.576	23,967,000 A
Emergency Federal Law Enforcement Assistance	16.577	3,000,000
Drug Control and System Improvement—Formula Grant	16.579	39,633,600 A
Other—Department of Justice	16.999	1,556,028
 Department of Labor:		
Labor Force Statistics	17.002	4,857,102
Employment Service	17.207	91,025,476 A
Unemployment Insurance	17.225	421,567,355 A
Senior Community Service Employment Program	17.235	6,598,244
Employment and Training Assistance—Dislocated Workers	17.246	70,034,198 A
Employment Services and Job Training—Pilot and Demonstration Programs	17.249	55,223
Job Training Partnership Act	17.250	329,283,220 A
Occupational Safety and Health	17.500	19,400,739

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Mine Health and Safety Grants	17.600	185,203
Disabled Veterans Outreach Program (DVOP)	17.801	9,330,237
Veterans Employment Program	17.802	921,750
Local Veterans Employment Representative Program	17.804	5,958,172
Other—Department of Labor	17.999	10,055,470

Department of State:

Other—Department of State	19.999	112,981
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Department of Transportation:

Boating Safety Financial Assistance	20.005	1,809,256
Aviation Education	20.100	80,804
Airport Improvement Program	20.106	81,395
Highway Planning and Construction	20.205	1,291,272,645 A
Motor Carrier Safety	20.217	2,450,105
Federal Transit Capital Improvement Grants	20.500	7,396,110
Federal Transit Technical Studies Grants	20.505	3,870,407
Federal Transit Capital and Operating Assistance Formula Grants	20.507	1,526,410
State and Community Highway Safety	20.600	17,280,619
Pipeline Safety	20.700	312,766

Footnotes are presented on page 198.

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
State Marine Schools	20.806	200,000
Other—Department of Transportation	20.999	502,121
Department of the Treasury:		
Exchange of Federal Tax Information With State Tax Agencies	21.004	347
Other—Department of the Treasury	21.999	63,113
Equal Employment Opportunity Commission:		
Employment Discrimination—State and Local Fair Employment Practices Agency Contracts	30.002	1,781,850
National Aeronautics and Space Administration:		
Aerospace Education Services Program	43.001	166,369
National Foundation on the Arts and the Humanities:		
Promotion of the Arts—Design Arts	45.001	371
Promotion of the Arts—Arts in Education	45.003	98,800
Promotion of the Arts—Media Arts: Film/Radio/Television	45.006	9,708
Promotion of the Arts—State and Regional Program	45.007	774,800

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Promotion of the Arts—Local Arts Agencies Program	45.023	100,000
Promotion of the Humanities—Summer Seminars for College Teachers	45.116	300,859
Promotion of the Humanities—NEH/Reader's Digest Teacher Scholar Program	45.154	8,250
National Science Foundation:		
Engineering Grants	47.041	19,629
Mathematical and Physical Sciences	47.049	1,643,848
Geosciences	47.050	198,584
Biological, Behavioral, and Social Sciences	47.051	65,746
Computer and Information Science and Engineering	47.070	96,236
Science and Technology Centers	47.073	232,611
Social, Behavioral, and Economic Sciences	47.075	74,422
Education and Human Resources	47.076	1,171,929
Small Business Administration:		
Business Development Assistance to Small Business	59.005	12,500
Procurement Assistance to Small Businesses	59.009	1,438,397
Small Business Development Center	59.037	2,492,803

Footnotes are presented on page 198.

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Department of Veterans Affairs:		
Grants to States for Construction of State Home Facilities	64.005	6,520,248
Veterans State Domiciliary Care	64.014	2,737,080
Veterans State Nursing Home Care	64.015	4,754,666
Veterans State Hospital Care	64.016	100,499
All-Volunteer Force Education Assistance	64.124	33,637
Other—Department of Veterans Affairs	64.999	758,922
Environmental Protection Agency:		
Air Pollution Control Program Support	66.001	2,401,739
Air Pollution Control—Technical Training	66.006	127,000
Air Pollution Control—National Ambient Air and Source Emission Data	66.007	126,935
State Indoor Radon Grants	66.032	76,592
Construction Grants for Wastewater Treatment Works	66.418	570,294
Water Pollution Control—State and Interstate Program Support	66.419	3,178,010
State Underground Water Source Protection	66.433	1,166,090
Water Pollution Control—Lake Restoration Cooperative Agreements	66.435	154,773
Construction Management Assistance	66.438	1,280,620

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Water Quality Management Planning	66.454	1,596,490
National Estuary Program	66.456	1,129,427
Capitalization Grants for State Revolving Funds	66.458	97,218,302 A
Nonpoint Source Reservation	66.459	147,288
Nonpoint Source Implementation 1 Grants	66.460	4,591,406
Wetlands Protection—State Development Grants	66.461	148,322
National Pollutant Discharge Elimination System Related State Program Grants	66.463	77,419
Air Pollution Control Research	66.501	11,937
Water Pollution Control—Research, Development and Demonstration	66.505	65,000
Safe Drinking Water Research and Demonstration	66.506	2,917,227
Toxic Substances Compliance Monitoring Program	66.701	191,048
Hazardous Waste Management State Program Support	66.801	6,802,481
Hazardous Substance Response Trust Fund	66.802	5,048,608
State Underground Storage Tanks Program	66.804	246,138
Underground Storage Tank Trust Fund Program	66.805	6,464,006

Footnotes are presented on page 198.

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Pollution Prevention Grants Program	66.900	64,883
Other—Environmental Protection Agency	66.999	441,635

Action:

Foster Grandparent Program	72.001	1,370,509
Senior Companion Program	72.008	19,001

Department of Energy:

State Energy Conservation	81.041	1,489,045
Weatherization Assistance for Low-Income Persons	81.042	5,769,488
Energy Extension Service	81.050	349,517
Energy Conservation for Institutional Buildings	81.052	479,825
Regional Biomass Energy Programs	81.079	24,579
Environmental Restoration	81.092	1,631,936
Science and Engineering Research Semester	81.097	124,528
Other—Department of Energy	81.999	123,000

Federal Emergency Management Agency:

Flood Insurance	83.100	179,841
Acquisition of Flood-Damaged Structures	83.104	94,248

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Civil Defense—State and Local Emergency Management Assistance	83.503	4,866,934
Disaster Assistance	83.516	143,322,139 A
Earthquake Hazards Reduction Grants	83.521	2,029,712
National Urban Search and Rescue (US&R) Program	83.526	61,496
Emergency Management Institute—Field Training Program	83.528	492,501
State and Local Emergency Management Assistance—Other Assistance	83.531	949,060
Facilities and Equipment	83.532	151,189
Other—Federal Emergency Management Agency	83.999	45,000
 Department of Education:		
Adult Education—State Administered Basic Grant Program	84.002	14,146,391
Bilingual Education	84.003	1,278,516
Desegregation Assistance, Civil Rights Training, and Advisory Services	84.004	500,493
Federal Supplemental Educational Opportunity Grants	84.007	65,116
Education of Handicapped Children in State Operated or Supported Schools	84.009	1,969,665
Chapter 1 Programs—Local Educational Agencies	84.010	541,245,418 A

Footnotes are presented on page 198.

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Migrant Education—Basic State Formula Grant Program	84.011	98,850,025 A
Educationally Deprived Children—State Administration	84.012	5,823,713
Chapter 1 Program for Neglected and Delinquent Children	84.013	3,569,080
Special Education—Innovation and Development	84.023	113,518
Services for Children With Deaf—Blindness	84.025	597,146
Special Education—State Grants	84.027	190,367,022 A
Special Education—Special Education Personnel Development and Parent Training	84.029	1,188,762
Guaranteed Student Loans	84.032	221,892,973 A
Federal Work-Study Program	84.033	19,719
Public Library Services	84.034	6,736,037
Interlibrary Cooperation and Resource Sharing	84.035	1,941,232
Federal Perkins Loan Program—Federal Capital Contributions	84.038	45,101
Vocational Education—Basic Grants to States	84.048	78,528,489 A
Vocational Education—Consumer and Homemaking Education	84.049	2,872,001
Vocational Education—State Councils	84.053	471,836
Federal Pell Grant Program	84.063	230,791

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Higher Education—Veterans Education Outreach Program	84.064	1,963
Grants to States for State Student Incentives	84.069	12,187,955
Special Education—Severely Disabled Program	84.086	77,648
Rehabilitation Services—Basic Support	84.126	147,431,598 A
Rehabilitation Services—Service Projects	84.128	1,289,100
Rehabilitation Training	84.129	460,805
Centers for Independent Living	84.132	599,699
National Institute on Disability and Rehabilitation Research	84.133	98,345
Federal, State, and Local Partnerships for Educational Improvement	84.151	50,292,839 A
Public Library Construction and Technology Enhancement	84.154	647,033
Secondary Education and Transitional Services for Youth With Disabilities	84.158	585,758
Disabled—Special Studies and Evaluation	84.159	109,077
Emergency Immigrant Education	84.162	6,687,308
Eisenhower Mathematics and Science Education—State Grants	84.164	24,770,190 A
Independent Living Services	84.169	880,633
Special Education—Preschool Grants	84.173	34,429,262 A

Footnotes are presented on page 198.

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Vocational Education—Community Based Organizations	84.174	1,496,833
Douglas Teacher Scholarships	84.176	2,719,542
Grants for Infants and Toddlers With Disabilities	84.181	8,821,000
Drug-Free Schools and Communities— National Programs	84.184	52,624
Robert C. Byrd Honors Scholarships	84.185	1,010,511
Drug-Free Schools and Communities— State Grants	84.186	51,757,153 A O
Supported Employment Services for Individuals With Severe Disabilities	84.187	3,821,604
Adult Education for the Homeless	84.192	503,957
Education for Homeless Children and Youth—Grants for State and Local Activities	84.196	1,069,664
College Library Technology and Cooperation Grants	84.197	111,753
Jacob K. Javits Gifted and Talented Students Education Grant Program	84.206	350,058
Even Start—State Educational Agencies	84.213	5,382,448
Even Start—Migrant Education	84.214	168,956
The Secretary's Fund for Innovation in Education	84.215	334,040
Capital Expenses	84.216	1,112,607
State Program Improvement Grants	84.218	2,006,247

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Student Literacy Corps and Student Mentoring Corps Programs	84.219	63,670
English Literacy Program	84.223	395,789
Mid-Career Teacher Training	84.232	57,138
Tech-Prep Education	84.243	3,463,677
Foreign Languages Assistance	84.249	259,032
Supplementary State Grants for Facilities, Equipment, and Other Program Improvement Activities	84.253	715,567
Grant Back Awards	84.995	147,992
Other—Department of Education	84.999	20,838
Consumer Product Safety Commission:		
Other—Consumer Product Safety Commission	87.999	13,800
Department of Health and Human Services:		
State Comprehensive Mental Health Service Planning Development Grants	13.158	1,013
Special Programs for the Aging—Title III, Part 6—Prevention of Abuse, Neglect and Exploitation of Older Individuals	93.041*** (93.552)	589,664
Special Programs for the Aging—Title III, Part A—Long-Term Care Ombudsman Services for Older Individuals	93.042*** (93.553)	400,647

Footnotes are presented on page 198.

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Special Programs for the Aging—Title III, Part F—Preventive Health Services	93.043*** (93.555)	686,297
Special Programs for the Aging—Title III, Part B—Grants for Supportive Services and Senior Centers	93.044*** (93.633)	28,712,470 A
Special Programs for the Aging—Title III, Part C—Nutrition Services	93.045*** (93.635)	42,202,465 A
Special Programs for the Aging—Title III, Part D—In-Home Services for Frail Older Individuals	93.046*** (93.641)	673,203
Special Programs for the Aging—Title IV—Training, Research and Discretionary Projects and Programs	93.048*** (93.668)	105,525
Food and Drug Administration—Research	93.103	145,132
Maternal and Child Health Federal Consolidated Programs	93.110	32,300
Biological Response to Environmental Health Hazards	93.113	19,956
Project Grants and Cooperative Agreements for Tuberculosis Control Programs	93.116	1,116,822
Acquired Immunodeficiency Syndrome (AIDS) Activity	93.118	10,484,625
Mental Health Planning and Demonstration Projects	93.125	327,527

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Emergency Medical Services for Children	93.127	40,746
Injury Prevention and Control Research and State Grants Projects	93.136	383,000
Minority Community Health Coalition Demonstration	93.137	28,715
Projects for Assistance in Transition from Homelessness (PATH)	93.150	4,721,876
Health Program for Toxic Substances and Disease Registry	93.161	558,880
Grants for State Loan Repayment	93.165	317,099
Community Youth Activity Demonstration Grants	93.170	52,162
Community Youth Activity Block Grants	93.171	5,118
Drug Abuse Treatment Waiting List Reduction Grants	93.175	477,531
State Data Collection—Uniform Alcohol and Drug Abuse Data	93.179	528,351
Cooperative Agreements for Drug Abuse Treatment Improvement Projects in Target Cities	93.196	4,654,659
HIV Home and Community-Based Health Services	93.199	393,186
Mental Health Research Grants	93.242	590,776
Mental Health Clinical or Service Related Training Grants	93.244	80,182
Childhood Immunization Grants	93.268	3,392,871

Footnotes are presented on page 198.

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Centers for Disease Control and Prevention—Investigations and Technical Assistance	93.283	1,701,530
Biomedical Research Support	93.337	291,125
Professional Nurse Traineeships	93.358	252,370
Cancer Detection and Diagnosis Research	93.394	86,830
Cancer Control	93.399	141,951
Emergency Protection Grants—Substance Abuse	93.554	100,658
Family Support Payments to States—Assistance Payments	93.560*** (93.020)	3,196,053,467 A
Job Opportunities and Basic Skills Training	93.561*** (93.021)	80,547,681 A
Assistance Payments—Research	93.562*** (93.022)	83,865
Child Support Enforcement	93.563*** (93.023)	195,522,050 A
State Legalization Impact Assistance Grants	93.565*** (93.025)	1,295,849
Refugee and Entrant Assistance—State Administered Programs	93.566*** (93.026)	85,893,697 A
Low-Income Home Energy Assistance	93.568*** (93.028)	64,688,698 A
Community Services Block Grant	93.569*** (93.031)	29,431,055 A

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Community Services Block Grant Discretionary Awards—Community Food and Nutrition	93.571*** (93.033)	466,200
Emergency Community Services for the Homeless	93.572*** (93.034)	1,562,402
Payments to States for Child Care Assistance	93.575*** (93.037)	50,556,521 A
Refugee and Entrant Assistance—Discretionary Grants	93.576*** (93.038)	214,686
Developmental Disabilities Basic Support and Advocacy Grants	93.630	5,770,000
Child Welfare Services—State Grants	93.645	38,148,035 A
Adoption Opportunities	93.652	1,368
Temporary Child Care and Crisis Nurseries	93.656	407,071
Foster Care—Title IV-E	93.658	454,909,238 A
Adoption Assistance	93.659	33,496,116 A
Social Services Block Grant	93.667	331,370,653 A
Child Abuse and Neglect Discretionary Activities	93.670	133,661
Family Violence Prevention and Services	93.671	1,097,839
Child Abuse and Neglect State Prevention Grants	93.672	487,283

Footnotes are presented on page 198.

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Grants to States for Planning and Development of Dependent Care Programs	93.673	1,211,276
Independent Living	93.674	9,976,527
Medicare—Hospital Insurance	93.773	2,120,608
Medicare—Supplementary Medical Insurance	93.774	12,886,356
State Medicaid Fraud Control Units	93.775	6,695,075
State Survey and Certification of Health Care Providers and Suppliers	93.777	17,285,399
Medical Assistance Program	93.778	6,834,508,609 A O
Health Care Financing Research, Demonstration and Evaluations	93.779	127,453
Social Security—Disability Insurance	93.802	127,436,416 A
Cellular and Molecular Basis of Disease Research	93.863	174,600
Model Comprehensive Drug Abuse Treatment Programs for Critical Populations	93.902	6,948,724
Model Criminal Justice Drug Abuse Treatment—Incarcerated Populations—Nonincarcerated Populations and Juvenile Justice Populations	93.903	426,226
Grants to States for Operations of Offices of Rural Health	93.913	80,400
HIV Care Formula Grants	93.917	16,046,285

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Cooperative Agreements for State-Based Comprehensive Breast and Cervical Cancer Early Detection Programs	93.919	1,505,600
HIV/AIDS and Related Diseases Among Substance Abusers: Community-Based Outreach and Intervention Demonstration Program	93.949	1,439,804
Demonstration Grants to States With Respect to Alzheimer's Disease	93.951	76,000
Block Grants for Prevention and Treatment of Substance Abuse	93.959	83,832,142 A O
Preventive Health Services—Sexually Transmitted Diseases Control Grants	93.977	2,238,354
Mental Health Disaster Assistance and Emergency Mental Health	93.982	3,722,654
Health Programs for Refugees	93.987	564,211
Cooperative Agreements for State-Based Diabetes Control Programs and Evaluation of Surveillance Systems	93.988	143,500
Preventive Health and Health Services Block Grant	93.991	6,433,805
Alcohol and Drug Abuse and Mental Health Services Block Grant	93.992	107,171,323 A O
Maternal and Child Health Services Block Grant to the States	93.994	39,543,152 A
Other—Department of Health and Human Services	93.999	6,294,751

Footnotes are presented on page 198.

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Commission on National and Community Service:		
Serve America/Higher Education	94.001	1,450,964
Miscellaneous Grants and Contracts:		
Shared Revenue—Flood Control Lands	98.002	213,063
Shared Revenue—Grazing Land	98.004	215,237
Federal Unemployment Benefits and Allowances	98.010	121,267
Department of Housing and Urban Development—College Housing Debt Service	98.013	1,239,265
Department of the Interior—Fire Prevention/Suppression Agreement	98.014	11,785
Department of the Interior—Fire Prevention/Suppression Agreement	98.015	493,529
Department of Agriculture and Various Other Departments—Fire Prevention/Suppression Agreements	98.016	12,038,017

<u>Federal Agency/Program Title</u>	<u>Federal Catalog Number</u>	<u>Grant Amounts Received</u>
Miscellaneous Federal Receipts	98.099	299,178
Miscellaneous Federal Receipts	98.999	<u>1,811,479</u>
Total Grants Received		<u>\$19,881,092,097</u>
Total Major Grants Audited in Compliance With OMB, Circular A-128		<u>\$19,324,079,665</u>

Note: In addition, the State received \$15,908,043 in Petroleum Violation Escrow Funds that can be used to supplement five federal energy-related conservation and assistance programs or for various federally-approved projects. The funds were audited to the extent required by the OMB's Circular A-128.

- A - The Bureau of State Audits reviewed these major grants for fiscal year 1992-93 in compliance with the OMB's Circular A-128.
- O - The Bureau of State Audits reviewed these grants in conjunction with various reports issued from July 1, 1992 to December 31, 1993. See the Schedule of Audit Reports Involving Federal Grants from July 1, 1992 to December 31, 1993, beginning on page 203 for a description of these reports.
- * - This amount includes cash and the value of commodities or cash and the value of food stamps.
- ** - This amount represents the value of commodities only.
- *** - The federal government changed the federal catalog number for fiscal year 1992-93. The number in parentheses represents the former federal catalog number.

**Weaknesses in Compliance With Federal Regulations
by Grant Program**

Federal Catalog Number	Grantor Agency/Program Title	Administering State Agency	Page Number	Weaknesses and Item Numbers ^a			
				Inaccurate/ Inadequate/ Late Reports	Insufficient Support for Expenditures	Insufficient Monitoring/ Auditing	Early Request/Late Disbursement of Federal Funds
Department of Agriculture							
10.550	Food Distribution	California Department of Education	78				8,9
10.553	School Breakfast Program	California Department of Education	78				11
		Department of the Youth Authority	163				1,2
10.555	National School Lunch Program	California Department of Education	78				11
		Department of the Youth Authority	163				1,2
10.557	Special Supplemental Food Program for Women, Infants, and Children	Department of Health Services	127	10			5,7,10
Department of Housing and Urban Development							
14.228	Community Development Block Grants/State's Program	Department of Housing and Community Development	47	4	2,3,5		1,6
Department of Justice							
16.579	Drug Control and System Improvement—Formula Grant	Office of Criminal Justice Planning	97	2	7,9	3 - 4	8

^aThe item number is the number of each weakness as presented in the report on each state agency.

		Weaknesses and Item Numbers ^a						
Federal Catalog Number	Grantor Agency/Program Title	Administering State Agency	Page Number	Inaccurate/ Inadequate/ Late Reports	Insufficient Support for Expenditures	Insufficient Monitoring/ Auditing	Early Request/Late Disbursement of Federal Funds	Other
Department of Labor								
17.225	Unemployment Insurance	Employment Development Department	118	4			5	
17.250	Job Training Partnership Act	California Department of Education	78			7		
		Employment Development Department	118			1 - 3	3	
Department of Transportation								
20.205	Highway Planning and Construction	Department of Transportation	59	2			3	
Federal Emergency Management Agency								
83.516	Disaster Assistance	Office of Emergency Services	147			1 - 3		
Department of Education								
84.010	Chapter 1 Programs—Local Educational Agencies	California Department of Education	78			13		
84.032	Guaranteed Student Loans	California Student Aid Commission	72	5 - 6	1			
84.151	Federal, State, and Local Partnerships for Educational Improvement	California Department of Education	78			13		

^aThe item number is the number of each weakness as presented in the report on each state agency.

Federal Catalog Number	Grantor Agency/Program Title	Administering State Agency	Page Number	Weaknesses and Item Numbers ^a			
				Inaccurate/ Inadequate/ Late Reports	Insufficient Support for Expenditures	Insufficient Monitoring/ Auditing	Early Request/Late Disbursement of Federal Funds - Other
84.164	Eisenhower Mathematics and Science Education—State Grants	California Department of Education	78	6	5 - 6		
		California Postsecondary Education Commission	68	2	1,5	4	
84.186	Drug-Free Schools and Communities—State Grants	Alcohol and Drug Programs, Department of	115	3	1 - 2		
		California Department of Education	78	14			
Department of Health and Human Services							
93.044 (93.633)*	Special Programs for the Aging—Title III, Part B—Grants for Supportive Services and Senior Centers	Department of Aging					
93.045 (93.635)*	Special Programs for the Aging—Title III, Part C—Nutrition Services	Department of Aging	113	1	2		
93.560 (93.020)*	Family Support Payments to States—Assistance Payments	Department of Social Services	141	3			
93.561 (93.021)*	Job Opportunities and Basic Skills Training	Department of Social Services	141				
93.566 (93.026)*	Refugee and Entrant Assistance—State Administered Programs	Department of Health Services	127	10			
93.575 (93.037)*	Payments to States for Child Care Assistance	California Department of Education	78			2	1
93.658	Foster Care—Title IV-E	Department of Social Services	141	3			
93.667	Social Services Block Grant	Department of Social Services	141				3

^aThe item number is the number of each weakness as presented in the report on each state agency.

*The federal government changed the federal catalog number for fiscal year 1992-93. The number in parentheses represents the former federal catalog number.

Federal Catalog Number	Grantor Agency/Program Title	Administering State Agency	Page Number	Weaknesses and Item Numbers ^a			
				Inaccurate/Inadequate/ Late Reports	Insufficient Support for Expenditures	Insufficient Monitoring/ Auditing	Early Request/Late Disbursement of Federal Funds
93.778	Medical Assistance Program	Department of Health Services	127				10
		Department of Mental Health	138				3
93.802	Social Security—Disability Insurance	Department of Social Services	141				1
93.959	Block Grants for Prevention and Treatment of Substance Abuse	Department of Alcohol and Drug Programs	115				3
93.992	Alcohol and Drug Abuse and Mental Health Services Block Grant	Department of Alcohol and Drug Programs	115				1
		Department of Mental Health	138				1 - 2
93.994	Maternal and Child Health Services Block Grant to the States	Department of Health Services	127				4
		Department of Health Services	127				10
Various Federal Departments							
	Numerous Federal Programs	Department of Finance	105				3
	Numerous Federal Programs	Department of Health Services	127				2
	Numerous Federal Programs	Health and Welfare Agency Data Center	124				1
	Numerous Federal Programs	California Department of Education	78				10
	Numerous Federal Programs	Department of Social Services	141				3
	Numerous Federal Programs	Stephen P. Teale Data Center	53				2
	Numerous Federal Programs	Department of General Services	154				1

^aThe item number is the number of each weakness as presented in the report on each state agency.

**Schedule of Audit Reports
Involving Federal Grants From
July 1, 1992 to December 31, 1993**

From July 1, 1992 to December 31, 1992, the Office of the Auditor General* issued reports on audits involving federal grants. From July 1, 1993 to December 31, 1993, the Bureau of State Audits issued reports on audits involving federal grants. The following schedule lists the reports issued and presents a summary of the report findings. The agencies' responses to these findings are included in each of the separate audit reports.

Agency Receiving Federal Funds	Federal Grant and Federal Catalog Number	Report Title and Description
Health Services, Department of	Medical Assistance Program 93.778	The Department of Health Services' Information on Drug Treatment Authorization Requests (P-213, 7-22-92) (1) During the six-month period from December 1991 through May 1992, the Department of Health Services (department) received approximately 91,000 drug treatment authorization requests (TARs) by mail, telephone facsimile machine, and the department's automated voice response system. This represents an increase of more than 12,500 drug TARs since our first review, which covered June 1990 through November 1990. (2) The department's backlog of drug TARs received by mail increased to approximately 8,900 by the end of May 1992. In comparison, at the end of November 1990, the department's backlog of unprocessed drug TARs was approximately 2,300 and, at the end of November 1991, approximately 5,500.

*The Office of the Auditor General was closed in December 1992. The California Government Code, Section 8543, creates the Bureau of State Audits. The Bureau of State Audits is responsible for performing the annual financial and compliance audit of the State and other audits formerly conducted by the Office of the Auditor General.

Agency Receiving Federal Funds	Federal Grant and Federal Catalog Number	Report Title and Description
University of California	Various federal grants	<p>A Review of the University of California's Executive Compensation, Benefits, and Offices (P-215, 8-26-92)</p> <p>(1) In an attempt to improve the University of California's (UC) executive compensation to make it more competitive with the compensation of other executives, the Regents of the University of California (regents) have approved a number of salary increases since 1983. For example, of ten executives in our sample, one had an increase of 10 percent, and nine had increases ranging from 21.3 percent to 40 percent between July 1983 and July 1984. Additionally, the regents may have approved some salary increases for fiscal year 1984-85 that were actually larger than they may have believed because the information presented in the document used to propose the increases lacked sufficient detail.</p> <p>(2) In addition to the regular contributions to the University of California Retirement Plan, the UC has provided a number of special retirement programs to the UC executives including nonqualified deferred income plans (NDIP). Although the regents have approved all the NDIPs, we found that materials presented to the regents were not always specific as to the amounts that would actually be paid. Consequently, we could not conclude that the regents knew the full extent of what they were approving or whether the UC staff correctly interpreted the regents' intent when they implemented the NDIP programs.</p> <p>(3) We noted several other areas of concern regarding policies and procedures for benefits to UC executives. Such areas included reimbursement of moving expenses, allowable entertainment costs, travel expenses, and others.</p>

Agency Receiving Federal Funds	Federal Grant and Federal Catalog Number	Report Title and Description
Alcohol and Drug Programs, Department of	Drug Free Schools and Communities— State Grants 84.186	<p>A Review of the Accomplishment of Goals Designed To Reduce Drug and Alcohol Abuse in California (93017, 9-23-93)</p> <p>(1) Provisions have been added to the California Health and Safety Code designed to reduce drug and alcohol abuse in California, improve the coordination of efforts to reduce drug and alcohol abuse, and provide direction for public policy decisions affecting drug and alcohol services.</p> <p>(2) Division 10.6 of the Health and Safety Code, Section 11998.1, sets forth 79 long-term five-year goals that focus on the elimination of drug and alcohol abuse in California. State agencies and counties share responsibility for 13 of these goals, with state departments solely responsible for 27 goals and counties solely responsible for 39 of the 79 goals.</p> <p>(3) State agencies have fully achieved 13 of the 40 goals they could address. Additionally, state agencies have made partial progress in meeting 22 of the goals. However, they have made no progress on 5 of the 40 goals they could address.</p> <p>(4) The Department of Alcohol and Drug Programs (department) provides guidance and funding to the counties for the development of county master plans. In our review of a sample of ten county master plans, we found that all ten master plans contain a description of the county's master plan advisory body as required by the State's guidance.</p> <p>(5) All 58 counties in the State are in some stage of developing a master plan for reducing drug and alcohol abuse. However, with few exceptions, information on the counties' progress in meeting the goals they could address is not available at the department because the department does not believe it has the statutory power to require such information.</p>

Agency Receiving Federal Funds	Federal Grant and Federal Catalog Number	Report Title and Description
Health Services, Department of	Medical Assistance Program 93.778	<p>The Department of Health Services' Information on Drug Treatment Authorization Requests (93012, 10-5-93)</p> <p>(1) From June 1992 through May 1993, the Department of Health Services (department) processed approximately 33 percent more drug treatment authorization requests (TARS) than it did in the first year of our review. In addition, the department's monthly backlog of drug TARS received by mail increased to approximately 5,000 in May 1993. In comparison, at the end of May 1991, the department's backlog of drug TARS received through the mail was approximately 2,900.</p> <p>(2) During the 12-month period from June 1992 through May 1993, the department reported that its average time for processing mailed drug TARS exceeded the 5 days state law requires. In May 1993, it took an average of 16 days to process mailed-in drug TARS.</p> <p>(3) In April 1993, the department contracted with nine pharmacist consultants to enable the drug units to process drug TARS more effectively and promptly. The department also hired two full-time pharmacist consultants to staff a new drug unit in San Bernardino. Their role is to process drug TARS by either approving, denying, modifying, or returning the TARS to providers (to request additional information).</p> <p>(4) From June through November 1992, the department was not processing drug TARS received by telephone facsimile machine within 24 hours, as federal law requires. However, for drug TARS received during May 1993, after the department contracted with nine pharmacist consultants, we found the department met the 24-hour requirement.</p>

**Schedule of Minor Federal Issues for the
Fiscal Year Ended June 30, 1993**

Agency Receiving Federal Funds	Federal Grant and Federal Catalog Number	Description of Issue
All		(1) The Department of Finance and the Public Employees' Retirement System did not always comply with administrative requirements of the federal government. Specifically, we noted that the Department of Finance made minor errors resulting in an overstatement totaling approximately \$300 in calculating the costs of its central service functions. In addition, we determined that the Public Employees' Retirement System incorrectly calculated the costs of its central service function resulting in an understatement totaling about \$7,000.
Alcohol and Drug Programs, Department of State Grants	84.186	(1) The department took more than 5 days to file claims with the State Controller's Office (SCO) for 3 of the 20 claim schedules that we reviewed. Specifically, the number of days between the date funds were drawn down and the date the department filed a claim with the SCO ranged from 7 to 8 days.
Motor Carrier Safety, State and Community Highway Safety and Other—Department of Treasury	20.217 20.600 21.999	(1) The CHP's drug-free workplace policies do not meet all the requirements of the Drug-Free Workplace Act.
California Highway Patrol		(1) The department made clerical errors that resulted in inaccurate meal counts. As a result of the inaccurate meal counts, the department overcharged the federal government by \$1,660.
Developmental Services, Department of School Breakfast Program and National School Lunch Program	10.553 10.555	

Agency Receiving Federal Funds	Federal Grant and Federal Catalog Number	Description of Issue
Economic Opportunity, Department of	National School Lunch Program 10.555	<p>(2) During fiscal year 1992-93, the department conducted six of eight required on-site monitoring reviews from 23 to 88 days late.</p>
Low-Income Home Energy Assistance 93.568 (93.028)*		<p>(1) The department did not always ensure that subrecipients submitted monthly reports on time. Specifically, two of five contractors submitted expenditure reports to the department from two to four weeks late.</p> <p>(2) The department submitted two late reports to the federal government; one report was 3 days late and the other was 18 days late.</p> <p>(3) The department issued a duplicate payment to one of its contractors. The contractor subsequently returned the payment to the department.</p> <p>(4) On June 30, 1993, the department had a cash balance of \$173,458 (5.1 percent of \$3.4 million in available federal funds) in excess of its immediate needs. The department cleared this excess balance by December 15, 1993.</p>
Low-Income Home Energy Assistance and Community Services Block Grant 93.568 (93.028)* 93.569 (93.031)*		<p>(1) The department failed to record two inventory adjustments and to retain two Notice of Arrival documents in its files.</p> <p>(2) The department was not aware that it did not receive a shipment of commodities that it requisitioned from the U.S. Department of Agriculture.</p>
Food Distribution 10.550		
Education, California Department of		

*The federal government changed the federal catalog number for fiscal year 1992-93. The number in parentheses represents the former federal catalog number.

Agency Receiving Federal Funds	Federal Grant and Federal Catalog Number	Description of Issue
School Breakfast Program and National School Lunch Program 10.553 10.555	Chapter 1 Programs—Local Educational Agencies 84.010	<p>(3) One of the Corrective Action Plans (CAP) was not approved within 90 days of the review, as required. The CAP was not approved until 122 days after the review.</p> <p>(4) For 3 of 30 local educational agencies that we reviewed, the department did not ensure that it collected and included data on students served by compensatory education programs prior to submitting that information to the U.S. Department of Education.</p>
Emergency Medical Services Authority	Emergency Medical Services for Children and Preventive Health and Health Services Block Grant 93.127 93.991	<p>(1) The authority does not have an ongoing policy for ensuring that its employees are aware of the requirements of the Drug-Free Workplace Act.</p>
Emergency Services, Office of	Disaster Assistance 83.516	<p>(1) The office did not submit 5 of 12 monthly cash transaction reports to the federal government on time.</p> <p>(2) The files for two recipients of disaster assistance funds did not contain all required forms.</p>
Health Services, Department of	Special Supplemental Food Program for Women, Infants, and Children 10.557	<p>(1) One of the 60 food vouchers we reviewed did not include the vendor name or number on the voucher. Redemption of vouchers without vendor name or number could result in redemption to unauthorized vendors.</p>
	Medical Assistance Program 93.778	<p>(2) The department overpaid an inpatient provider by \$307 because the incorrect reimbursement rate was used for an out-of-state inpatient hospital. Beginning March 1, 1992, the statewide average reimbursement rate was 61 percent, but an out-of-state inpatient hospital was reimbursed at 63 percent.</p>

Agency Receiving Federal Funds	Federal Grant and Federal Catalog Number	Description of Issue
Housing and Community Development, Department of	Community Development Block Grant 14.228	<p>(1) During a site visit of one of its subrecipients, the department failed to determine that funding for the grant had been completed and that the subrecipient had not submitted all financial and performance reports as required. Furthermore, the department did not determine that close-out procedures had not been performed.</p> <p>(2) The checklist the department developed to monitor subrecipients' compliance with civil rights requirements does not include a specific reference to discrimination based on religious preference.</p>
Justice, Department of	Drug Control and System Improvement— Formula Grant 16.579	<p>(1) Program performance reports are not filed with the Office of Criminal Justice Planning within 30 days of the end of the applicable period, as required.</p> <p>(2) The department's drug-free workplace policy does not fully meet the requirements of the Drug-Free Workplace Act.</p>
Rehabilitation, Department of	Rehabilitation Services—Basic Support 84.126	<p>(1) Two of 25 open case files we tested were not reviewed by the department within the required 90 days while the client was in extended evaluation.</p>

Agency Receiving Federal Funds	Federal Grant and Federal Catalog Number	Description of Issue
Social Services, Department of		
Child Support Enforcement	93.563 (93.023)*	(1) The department understated the federal share of expenditures for the quarter ended March 31, 1993, by approximately \$4,000. It corrected the error on the federal report for the quarter ended March 1994.
Job Opportunities and Basic Skills Training	93.561 (93.021)*	(2) The department held excessive federal monies, ranging from \$75 to approximately \$32,700 between the periods from January 31, 1992 to March 31, 1992, and from October 31, 1992 to November 30, 1992.
Refugee and Entrant Assistance—State Administered Programs	93.566 (93.026)*	(3) For 3 of the 12 cases that we reviewed, the department did not receive required progress or change of status reports from counties for unaccompanied minors served in the program.
Child Welfare Services—State Grants	93.645	(4) In January 1993, the department overcharged the federal government by approximately \$158 for its share of personal services costs of the child welfare services program. The department corrected the error in April 1994.
Foster Care—Title IV-E	93.658	(5) The department undercharged the federal government by approximately \$26 for its share of operating expenses of the foster care program.
Statewide Health Planning and Development, Office of		
Grants for State Loan Repayment and Health Care Financing Research, Demonstration and Evaluations	93.165	(1) The office does not have an ongoing policy for ensuring that its employees are aware of all requirements of the Drug-Free Workplace Act.
	93.779	

*The federal government changed the federal catalog number for fiscal year 1992-93. The number in parentheses represents the former federal catalog number.

Agency Receiving Federal Funds	Federal Grant and Federal Catalog Number	Description of Issue
Toxic Substances Control, Department of Transportation, Department of	Various Highway Planning and Construction 20.205	<p>(1) The department's drug-free workplace policies do not meet all the requirements of the Drug-Free Workplace Act.</p> <p>(1) The department coded a utility relocation payment of \$6,274.92 as federally reimbursable. However, the utility relocation agreement did not state that payments were reimbursable by the federal government. The department corrected the error in February 1994.</p> <p>(2) The department did not reverse a right-of-way expenditure involving federal funding for a condemnation deposit of \$89,500, which was refunded to the department. The department corrected this error in March 1994.</p>
Water Resources Control Board	Capitalization Grants for State Revolving Funds 66.458	<p>(1) The board did not enter into binding loan commitments of at least 120 percent of the quarterly grant payment previously received in the second, third, or fourth quarters for the state fiscal year ended June 30, 1993.</p> <p>(2) In its annual report, the board did not specify that it had deposited its match on or before the date on which each federal quarterly grant payment was made or that the State had expended all funds in an expeditious and timely manner.</p>

Report on Compliance With State Laws and Regulations



CALIFORNIA STATE AUDITOR

BUREAU OF STATE AUDITS

KURT R. SJOBERG
State Auditor

MARIANNE P. EVASHENK
Chief Deputy State Auditor

Independent Auditors' Report on Compliance With State Laws and Regulations

The Governor and the Legislature of
the State of California

We have audited the general purpose financial statements of the State of California as of and for the year ended June 30, 1993, and have issued our report thereon dated April 30, 1994. We did not audit the financial statements of the pension trust funds, which reflect total assets constituting 78 percent of the fiduciary funds. We also did not audit the financial statements of certain enterprise funds, which reflect total assets and revenues constituting 92 percent and 94 percent, respectively, of the enterprise funds. In addition, we did not audit the University of California funds. The financial statements of these pension trust funds, certain enterprise funds, and the University of California funds referred to above were audited by other auditors who furnished their reports to us, and our opinion, insofar as it relates to the amounts included for the pension trust funds, certain enterprise funds, and the University of California funds, is based solely upon the reports of other independent auditors.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the general purpose financial statements are free of material misstatement.

The State's management is responsible for compliance with laws, regulations, contracts, and grants applicable to the State of California. As part of obtaining reasonable assurance about whether the general purpose financial statements are free of material misstatement, we performed tests of the State of California's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our audit of the financial statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests indicate that, with respect to the items tested, the State of California complied, in all material respects, with the provisions referred to in the preceding paragraph. With respect to items not tested, nothing came to our attention that caused us to believe that the State of California had not complied, in all material respects, with those provisions. However, we noted certain immaterial instances of noncompliance that we have reported to the management of agencies of the State of California. We discuss these on pages 39 through 164 of this report.

This report is intended for the information of the Governor and Legislature of the State of California and the management of the executive branch. However, this report is a matter of public record, and its distribution is not limited.

BUREAU OF STATE AUDITS



SALLY L. FILLIMAN, CPA
Deputy State Auditor

April 30, 1994

**Appendix Reports Issued by the Office of the Auditor General*
and the Bureau of State Audits From
July 1, 1992 to December 31, 1993**

Date of Issue	Report Title	Report No.
<u>1992</u>		
Jul 01	A Review of Court Services in San Bernardino County	P-134
Jul 02	A Review of Selected Areas of the Chino Unified School District's Building Program	P-142
Jul 23	The Department of Health Services' Information on Drug Treatment Authorization Requests (Letter Report)	P-213
Aug 05	A Fiscal Impact Analysis of Undocumented Immigrants Residing in San Diego County	C-126
Aug 06	Public Reports of Investigation Completed by the Office of the Auditor General From January 1, 1991 Through July 31, 1992	I-214
Aug 26	A Review of the University of California's Executive Compensation, Benefits, and Offices	P-215
Sep 02	Some Counties Are Not Promptly Remitting to the State Fees Collected for the Judges' Retirement System	P-141
<u>1993</u>		
Sep 23	A Review of the Accomplishment of Goals Designed To Reduce Drug and Alcohol Abuse in California	93017
Oct 5	The Department of Health Services' Information on Drug Treatment Authorization Requests (Contract audit by The Thornton Group)	93012

*The Office of the Auditor General was closed in December 1992. The California Government Code, Section 8543, creates the Bureau of State Audits. The Bureau of State Audits is responsible for performing the annual financial and compliance audit of the State and other audits formerly conducted by the Office of the Auditor General.

Date of Issue	Report Title	Report No.
Oct 7	State of California, Statement of Securities Accountability of the State Treasurer's Office, June 30, 1992	92008
Dec 1	Review of the California Department of Toxic Substances Control's Implementation of the Hazardous Waste Source Reduction and Management Review Act of 1989 (Contract audit by Ernst & Young)	93018
Dec 28	State of California, Financial Report Year Ended June 30, 1992	92001
Dec 30	A Review of the Department of Motor Vehicles' Administration of the Collegiate License Plate Program	93022
Dec 31	A Review of the State's Controls Over Its Financial Operations	92002
Dec 31	State of California, Comprehensive Financial and Compliance Audit Report, Year Ended June 30, 1992	92003

DEPARTMENT OF FINANCE

OFFICE OF THE DIRECTOR
STATE CAPITOL, ROOM 1145
SACRAMENTO, CA 95814-4998



July 8, 1994

Mr. Kurt R. Sjoberg
State Auditor
660 J Street, Suite 300
Sacramento, Ca 95814

Dear Mr. Sjoberg:

CONTINUED IMPROVEMENT NEEDED IN THE STATE'S CONTROLS OVER ITS OPERATIONS

Thank you for the opportunity to respond to the statewide issues contained in your draft report, which was prepared as part of your examination of the State's general purpose financial statements for the Fiscal Year ended June 30, 1993. The findings in this report will be incorporated into the Single Audit Report filed with the federal government by the State of California covering Fiscal Year 1992-93.

We appreciate the information provided to us regarding the state's internal controls, and its compliance with federal and state requirements. Although our systems can always be improved, the fact that the cumulative findings do not adversely affect the State's general purpose financial statements is evidence that the State's operations are materially under control.

California is a complex entity with numerous programs and activities being carried out for its citizens. Such complexity, along with budget constraints, challenge us to assure effective control while considering the benefits and costs of these controls. However, improving the State's internal control structure will continue to be an important responsibility of the financial leadership of the State.

Each department for which you have identified internal control weaknesses is responsible for its own corrective action. Our department, however, will continue to provide the leadership necessary to assure the existence of an appropriate internal control structure and effective practices and procedures over fiscal and program operations. We will monitor the corrective actions to be taken by individual departments as necessary.

The following is our response to each of the statewide concerns that you have identified in your draft report.

POTENTIAL LIABILITY TO THE FEDERAL GOVERNMENT FOR SOME INTERNAL SERVICE FUNDS

As indicated in your report, the federal Department of Health and Human Services is currently conducting an audit of the methodology used by the internal service funds in question for the period of July 1, 1984 through June 30, 1991. We disagree with the preliminary findings of the federal audit in a number of areas. We have taken exception to the use of inconsistent federal participation ratios and think that federal participation should be based on actual ratios as determined by audit tests. In addition, we believe that the accumulated surplus of the funds in question should be reduced by the amounts of the reserve for prepaid items, of accrued liabilities for Workers Compensation costs, and of compensating absences for the Service Revolving Fund. We have notified the federal government of our concerns.

Also, we have requested the federal government to approve a working capital reserve of 60 days as noted in your report and as approved for the state of Oregon. The 60 days' reserve is part of the changes to the cost principles that the federal government is proposing. When those changes are finalized, the State will review its procedures and determine the practicality of changing our current system for Internal Service Funds, and updating the necessary guidelines.

USE OF ANTICIPATED SALARY SAVINGS

We do not dispute that the traditional process of using a Section 27 deficiency notification was not used in the case of the \$16.5 million noted in your report. However, the Legislature was notified and provided its approval of the actions taken through the 1994 May Revision Process. Staff from the Legislature, the Legislative Analyst's Office, the State Controller's Office and other interested agencies were also notified of the actions taken. We feel that these actions resolved this issue. We also feel that because this is presented as a statewide issue, that the total amount reported should include the \$12.8 million of IDDA/EPDA funds expended by the Legislature.

① *

LACK OF DOCUMENTATION OF DIFFERENCES IN ACCOUNTING PRACTICES

Some of the differences between the State Controller's figures and the Department of Finance figures may be attributable to timing differences and information received late from state agencies. However, we are not aware that any differences have impaired the integrity of the state's budgetary process.

*The California State Auditor's comments on this response begin on page 225.

Specific differences can be documented and explained for some items, but determining all of the differences would require a major reconciliation. As we become aware of significant differences, they will be addressed in relation to other priorities and existing resources. However, we do not currently have the resources to complete a reconciliation between our figures and the State Controller's figures.

PROBLEMS WITH THE STATE'S CONVERSION TO GAAP

We are continuing to address some of the Generally Accepted Accounting Principles (GAAP) issues. A committee has been formed including representatives of the Department of Finance, the State Controller's Office and your office. This committee has established and prioritized a preliminary list of accounting issues that will be analyzed for possible conversion to GAAP. Items that are approved by the committee and are determined to be in the best interests of the State will be converted to GAAP. However, there are some areas where GAAP treatment may not be practical or where the cost of establishing the necessary systems exceeds the benefits.

The State's legal or budgetary basis of accounting is converted each year by the State Controller's Office to a GAAP basis for reporting purposes. We are not aware of specific problems occurring with material impacts to the financial statement presentations during this process.

INADEQUATE MONITORING OF RECIPIENTS OF STATE AND FEDERAL MONEYS

The monitoring of recipients of federal funds is the responsibility of individual state agencies and specific requirements are found in Section 20050 of the State Administrative Manual (SAM). Required monitoring of State monies is usually detailed in enabling legislation. In order to emphasize the importance of this function we will reissue our Management Memo restating the necessity for this monitoring. In addition, the next update to the audit program for internal control audits will include a section on monitoring of State and Federal fund recipient organizations.

INADEQUATE REPORTING OF LEASING INFORMATION

As indicated in your report, there are some state agencies for which the Department of General Services (DGS) does not have oversight responsibility. In order to include the information for these entities in the DGS records, it will probably be necessary to make the submission of this information a legal requirement. The information currently included in DGS records does not include some of the information needed for the notes to the State's financial statements. Since the information currently maintained by DGS is primarily for internal management purposes, acquiring and maintaining additional information would be an increased cost to DGS.

It may not be cost effective to require the gathering and maintaining of this information for all departments. The DGS is currently addressing the issue of expanding their data base on leasing information to include additional information.

CONFUSION OVER REQUIREMENTS FOR APPROVAL FOR SOME CONTRACTS

As indicated in your report, approval of contracts is the responsibility of the Department of General Services (DGS). If there are agencies that are not complying with the Public Contract Codes, DGS should initiate corrective action. However, we aren't aware that there have been material losses or misuse of grant funds disbursed. We will notify the Department of General Services of your recommendation to obtain a current opinion from the Attorney General to clearly identify the factors distinguishing grants from contracts.

DEFICIENCIES IN ADMINISTERING STATE CONTRACTS

Your report identifies 13 contracts, out of 85 tested at 17 agencies, that lacked approval before the start of work. Of these 13, 9 were found in just 4 agencies. These 4 agencies all have an internal audit unit. The next update to the audit program for internal control audits will place more emphasis on reviewing contracting procedures. The audit program is provided to the internal auditors for them to use when conducting reviews of their department's internal controls.

FAILURE TO REQUIRE AGENCIES TO PREPARE RECONCILIATIONS OR REPORTS OF ACCRUALS

As indicated in your report, efforts are underway to make financial reporting more accurate and prompt. As part of this effort a determination will be made, as other priorities and resources allow, as to which year-end financial statements are necessary. Specifically, Report 15 contains summary information that is included on other required reports and is duplicated on Report 15.

(2)

LATE AUDITED FINANCIAL STATEMENTS - LACK OF COMBINING STATEMENTS BY FUND TYPE

Efforts are underway to reduce the time required by state agencies to prepare and submit the year-end statements to the State Controller's Office. The State Controller is working towards having statements be electronically submitted. In addition, a review is underway to reduce the number of different statements required which should reduce the time needed to prepare and submit statements.

INABILITY TO ACCOUNT FOR EXPENDITURES OF FEDERAL MONEY BY EACH FEDERAL PROGRAM

The accounting system currently used to record federal receipts and expenditures will need extensive modification to meet all federal and State requirements. The system does not currently allow a cross-over between receipts and subsequent expenditures by federal program. Required changes will be addressed in relation to other priorities and existing resources.

LACK OF CENTRALIZED RECORDS FOR FEDERAL RECEIPTS

As indicated in your report, the State established the Federal Trust Fund in 1978 for the deposit of all moneys received by the State from the federal government where the expenditure was administered through or under the direction of any state agency. Unfortunately, exemptions were also allowed. The necessary changes to statutes to achieve the objectives of the Federal Trust Fund will be analyzed as priorities and resources allow.

LACK OF COMPLIANCE WITH DRUG-FREE WORKPLACE REQUIREMENTS

Drug-Free workplace requirements for state employees are the responsibility of the Department of Personnel Administration (DPA). We will notify DPA of this issue and will recommend that they reissue a Management Memo to all state departments on the requirements of a drug-free workplace.

The requirement for certification by contractors is the responsibility of the DGS. We will notify DGS of this issue and will recommend that they remind state entities of the contractor requirements. We will also recommend to DGS that the delegated contracting audits conducted by DGS include a review of Drug-Free workplace certifications by contractors.

SALARY WARRANTS ARE NOT ALWAYS PROMPTLY RETURNED

State policy as detailed in Section 8580.5 of the State Administrative Manual requires undelivered salary warrants to be returned to the State Controller's Office within 90 days of receipt. In order to increase compliance with this policy, agencies will be reminded of this requirement through a Management Memo. In addition, the next update to the audit program for internal control audits will place more emphasis on this issue.

IMPROPER OMISSIONS FROM THE STATE REPORTING PROCESS

A Statement of Operations and a Budget Report are submitted annually by District Agricultural Associations to the Division of Fairs and Expositions within the Department of Food and Agriculture. However, Section 4005 of the Food and Agricultural Code states that the fiscal year for these entities is January 1, to December 31. Section 4505 of the Food and Agriculture Code requires a statement of operations to be filed on a calendar year basis. In order to include statements in the State Controller's annual report for these entities, the statute will have to be changed, or statements will have to be prepared twice a year at an additional cost. The necessary statutory changes will be analyzed as priorities and resources allow.

We appreciate the recommendations that you have identified regarding the state's operations. Our own efforts, as well as those of departmental internal auditors, have identified similar weaknesses. We are aware of efforts underway in a number of areas to correct these weaknesses. We will continue to provide the leadership to ensure the proper financial operations of the State.

If you have any questions concerning this letter, please contact Enrique Farias, Chief, Office of State Audits and Evaluations at 322-2917.

Sincerely,



RUSSELL S. GOULD
Director

California State Auditor's Comments on the Response From the Department of Finance

- ① We met with officials of the Department of Finance (department) on several occasions and were not provided with documentation indicating the Legislature's approval of these actions. Further, the department's response does not address the issue we raised that three departments were afforded a benefit not provided to other General Fund departments. Finally, Chapter 83, Statutes of 1991, specifically exempted the Legislature's 1991-92 appropriations from reduction.
- ② We agree that other reports supply some of the information provided in the Report 15. However, the funds that are exempted from providing a Report 15 to the State Controller's Office are also exempted from providing these other reports. Therefore, the State Controller's Office does not have evidence that agencies have reconciled financial information that appears in the State's general purpose financial statements with records of the State Controller's Office.

cc: **Members of the Legislature**
Office of the Lieutenant Governor
State Controller
Legislative Analyst
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
Senate Majority/Minority Consultants
Capitol Press Corps